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ROYAL COMMISSION
ON
CO-OPERATIVES

1945

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(OFFICIAL REPORT)

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add J. J. Vaughan Rep.

T. S. HUBBARD
OFFICIAL REPORTER

Mr. Vaughan

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ROYAL COMMISSION ON CO-OPERATIVES

Ottawa, Wednesday, April 18, 1945

Volume XX

(Pages 5902 - 6061)

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ROYAL COMMISSION ON CO-OPERATIVES

The Commission appointed to inquire into the present position of Co-operatives in the matter of income and excess profits tax, organization and business methods and operations, and the comparative position of persons engaged in business directly competitive therewith, met in Ottawa, on Wednesday, April 18, 1945.

PRESENT:

The Hon. Mr. Justice ERROL M. McDOUGALL, Chairman.

B.N. ARNASON)	
G.A. ELLIOTT)	
J.M. NADEAU	)	Commissioners.
J.J. VAUGHAN)	
Eugene T. Parker, K.C.	)	Associate
Roger Brossard, K.C.	)	Counsel
Major H.D. Woods	)	Associate
J.A. Chapdelaine	)	Registrars.
Colonel G.W. Ross	)	Executive
	)	Secretary.

APPEARANCES:

W.B. Francis,	Group of Co-operative Associations
W.H. Howard, K.C.,	Private Grain Interests
W.P. Fillimore, K.C.,	Private Grain Interests
R.H. Milliken, K.C.,	Saskatchewan Co-operatives
G.W. Mason, K.C.,	American Reciprocal Association
V. Evan Gray, K.C.,	Factory Mutual Fire Insurance Companies
Hon. S.A. Hayden, K.C.,	American Mutual Alliance
N.S. Robertson,	Ontario Cash Mutuals
Russell MacKenzie, K.C.,	Canadian Board of Marine Underwriters
J.A. Mann, K.C.)
Aime Geoffrion, K.C.)
A. Leslie Ham)
Jean-Paul Verschelden)
Dollard Dansereau)
	La Societe Mutuelle D'Assurances Generales de L'V.C.C.

LA SOCIETE MUTUELLE D'ASSURANCES
GENERALES de L'U.C.C.

(French - pp. 5904 - 5979)

AMERICAN MUTUAL ALLIANCE

MR. HAYDEN: I notice in looking at the transcript that I made one statement yesterday which was not accurate. I have no doubt I made it, since it is reported, but I should like to correct it. At page 5880, at the bottom of the page, I made the statement that 98 per cent of what I think I called the unabsorbed premium was returned to the policy holder. What I should have said was that 98 per cent of the net premiums was used in paying losses and expenses, and in the return or dividend to the policyholder, so that only 2 per cent of the net premium was held back by the company. That appears absolutely clear, even to the percentages, in the appendices; but for some reason or other I misstated it when I was making the statement on it.

Then in case there might be some confusion by reason of the fact that in appendix 4 there appears in connection with quite a number of these companies in some years, taking for instance appendix 4, page 3, dealing with the Indiana Lumbermens Mutual Insurance Company it shows that in the year 1943 that company, as far as its Canadian operation was concerned, had a minus underwriting gain; in other words it had an underwriting loss; yet they paid out moneys to the policyholders. The net result was that the minus balance went in. I wanted to direct your attention to the fact that this statement has lifted out of the larger company's statement, which covers the United States operation as well as Canadian, just the Canadian end of it. If in 1943, for instance, Canadian policyholders received a dividend at a time when, in relation to their premiums paid, the losses and expenses were so high that there was no underwriting gain, then it means that they got the benefit of being in a larger

group or a larger pool. So it does not mean that in the business of the company in that year, having regard to its United States and Canadian operations, there was any payment of dividend in excess of the underwriting gain. It just means that when you segregate the Canadian business, the Canadian policyholders had an advantage that year because the over-all picture was better than the Canadian picture. Since it is a pool; since it is a mutual insurance, they got their percentage of the over-all operation. It is one company.

The other thing I wanted to mention was that last evening I ventured the statement that the British and foreign corporations under the Income War Tax Act procedure or formula did not include as part of their taxable income their investment income. Having reviewed that situation in the interim I am in a position where I feel I can state that to be a fact. If there is any doubt about it, we can easily get some person from the income tax department to satisfy us on that.

THE CHAIRMAN: That is the point Mr. Glassco discussed with us this morning. We can get that information.

MR. HAYDEN: For the purposes of this inquiry, from my point of view I am stating it as a fact as strongly as I can. I have examined some of the statements as contained in the insurance reports.

While a previous counsel was presenting a brief there was some question of the relevancy of questions relating to the operations of the Special War Revenue Act for the purposes of this inquiry. If that question is to become important at any stage, I would reserve my right to argue the relevancy of it. As I understand it, at some time it is intended to hear argument?

THE CHAIRMAN: Well, after we complete this week and possibly next week I cannot see any room for any argument

coming then.

MR. HAYDEN: There are things that have not been said, certainly by me; I have stuck as closely as I could to statements of fact, on the understanding that at some stage argument might be presented.

THE CHAIRMAN: The arguments have been presented in the brief, and in other briefs, on that aspect of the case.

MR. HAYDEN: Well, the main brief presented by the clients whom I represent adheres as closely as possible to statements of fact; and the reply purports only to deal with certain what we regard to be misstatements of fact in the brief of the joint stock companies.

THE CHAIRMAN: I think we have almost promised final argument, if it is found necessary, either orally or later in writing.

MR. HAYDEN: In either form that would be satisfactory, but there are some views I have hesitated to take the time of the Commission in expressing, because I thought this part of the inquiry was to ascertain factually the position, and I have been trying to stay in that field.

Subject to these considerations I propose now to call Mr. Gruhn.

A. V. GRUHN

Of the City of Chicago, having been
duly sworn, testified as follows:

BY MR. HAYDEN:

Q. Mr. Gruhn, what is your position in relation to mutual insurance operation? A. Well, first I am the general manager of the American Mutual Alliance, which is a voluntary association of mutual fire and casualty companies doing business in the United States, a few of which operate

in Canada. The Alliance is composed of three constituent associations which work in cooperation, but which maintain individual identities, such as the Federation of Mutual Fire Insurance Companies, which is a voluntary association of mutual fire companies; the National Association of Mutual Casualty Companies, which is a voluntary association of mutual casualty insurance companies, and the National Association of Automotive Mutual Insurance Companies, which is an organization of automobile writing insurance companies. The American Mutual Alliance is the common organization through which they cooperate and function.

Q. Could you indicate some of the purposes?

A. I can state them exactly, as they are set out in the objects of the association, if you care to have them all.

Q. I do not want them all. I made the statement yesterday that the function of the American Mutual Alliance, for instance, related to making statements and representations at tax inquiries, for example?

A. Not only that. The objects are as follows:

"1. To provide a centralized organization for cooperation with and between the mutual fire and casualty insurance companies of the United States and to encourage cooperation among all such companies.

"2. To assist commissioners and superintendents of insurance and other state and federal supervisory authorities in all helpful ways in improving conditions in the insurance field and in raising and keeping the operation of the insurance business on a high plane in the interests of the insuring public.

"3. To encourage and promote adequate, reasonable and uniform legislation relating to mutual insurance and to the prevention and reduction of losses.

"4. To gather and collate information and experience concerning insurance, rates and hazards."

That is something we have not undertaken.

"5. To eliminate hazards, prevent and reduce losses and to cooperate with approved agencies for these purposes."

"6. To consider and recommend proper and desirable standards, methods, and practices, to encourage uniformity and to do any and all things necessary or incidental to the accomplishment of these objects to the end that the benefits of mutual insurance may be made available to every insurable risk."

"7. To give publicity through all available channels on the subject of mutual insurance."

Q. Are you acquainted with the operations of most mutual insurance companies in the United States?

A. In a general way, and I think for the purposes of this inquiry, as we understand it, I am. Of course, as to the minute details of every organization, I do not claim to have all that information.

Q. Are you directly connected with any mutual insurance company? A. Oh, no.

Q. Are all the American mutual insurance companies corporations? A. Yes. There are over 2,600 mutual fire and casualty companies in the United States. There may be a few old, special legislative charter companies remaining in business. If so I am not aware of them; but even down to the small local farm company, they are practically all incorporated.

Q. Then do most of the American mutuals operate in the same manner as these thirteen companies that have made their submission here through me? A. All mutual insurance companies operate in general on the same fundamental principles. There are incidents of operation which differ.

The vast majority of the companies, I think about 2,200 of them, city and town and farm and assessment companies in the United States, are all fundamentally mutual. The policyholders are members; but in their contribution of premiums to the companies, those incidents vary. As to the companies in general, commercial and dwelling house fields, which number the remainder between the more than 2,600 and this approximately 2,200 -- and those figures are given roughly -- they operate in general in the same manner as do the Alliance companies in Canada. The factory mutual method of operation in the field is limited to a small number of companies.

Q. There has been, I think I could say, a considerable discussion during the last several days, as to the form of the non-stock mutual companies or non-stock insurers, and whether that type of insurer is an association or a group for an organization or an enterprise, which I think was one word that was used, or a partnership or a corporation, and whether reserves are established and moneys invested and re-insurance arrangements entered into -- we have had all those factors gone into. I wonder if you would tell me what you have to say on those points, in so far as the mutual insurance operations are concerned?

A. Well, to cut through the various definitions and meanings that various individuals may apply to words or terms, and to eliminate the fact that in the common understanding of certain phases of insurance there are certain trade terms that have been developed which mean all things to some and some things to all, and a few things to a few, and that sort of thing; for the purpose of getting down to what I regard as the nub of this question, I will say this, pertaining to our companies, and by "our" companies I am

talking not in the possessive sense but in the sense that we engage together in a common purpose.

The mutual company is a company in which the policyholders make common cause in securing and furnishing their own insurance protection. Whether that common effort is in a corporate form or incorporated form or a partnership, whatever it might be, the purpose does not change by reason of the form of the organization which is the service office that collects the premiums, shall I say, and administers the funds. That work is done by managers selected by the boards of directors, who perform their duties in accordance with their instructions. All of these various insurance groups represent methods by which the policyholders combine for protection; and the policyholders combine and make contributions to pay losses and expenses, even in a stock company. But there the purpose of the corporation, the purpose of those who make common cause in the corporate entity, those who are the owners of the corporate entity, is to operate the service organization for their profit. That does not mean they do not render a valuable service.

BY THE CHAIRMAN:

Q. You can combine ~~profit~~ and service, can you not?

A. Oh, absolutely; that is what I am saying. If they did not furnish service; if they did not furnish protection, they would not exist. But the purpose of the organization is to make a profit for third-party interests, who are shareholders and who are interested in making a profit legitimately by rendering a service.

Please bear this in mind; that in a stock insurance Company the policyholder has not transferred his risk from himself to the shareholder. He still carries a large stake in the hazards of the enterprise, to the same degree and

probably in some cases to a greater degree than holders of equity capital where the enterprisers are supposed to carry the burdens and the responsibilities and the losses. They do not by any means furnish guaranteed protection, because in an insurance company, I do not care what kind it is, the policyholders pay in advance for something they may never get. The purchaser of an automobile, when he pays his money, gets an automobile. The equity shareholder of the corporation, be it an industrial or merchandising or ordinary distributing corporation, hazards that money, and he carries the sole hazard for its loss. But in a stock insurance company the hazard of the enterprise is shared by the policyholder, because he pays in advance. In case of failure he stands a chance of losing his premium; and if he has had a loss and there have been a number of losses, a series of losses, during the period while the company was going down, he may not be paid dollar for dollar the less for which he contracted when he gave his premium.

Now I want to say as to mutual companies, that they represent solely the policyholders. The policyholders make no investment in the company. They pay their premium, and I am using the word "premium" in the broadest sense in that it represents contribution that each policyholder makes to a common fund out of which the losses of the few are indemnified. The venture is in no way a profit venture. It is not organized for the purpose; it is not operated for the purpose.

Again to cut through and save a good many questions, there are reserves, of necessity, and I will go into that at the proper time. There are reserves, and there are surpluses. In the insurance business the protection of policyholders cannot be accomplished without reserves and

without surpluses, because you cannot cut off a company at the end of the day and know exactly dollar for dollar where you stand on both sides of the ledger. So the management of the mutual companies adopts all the modern conveniences of business, from the most efficient statistical machinery and typewriters and all the rest of it to the other mechanics of conducting an insurance business. We invest the reserves; and by "we" I am speaking again of the management. We invest the reserves and hope to realize a return on them. We can leave them in the drawer, or under the insurance mattress, but that would not be in the interests of the policyholders. So we have receipts from investment income, rents and all the rest of it. Please understand that.

We engage in the exchange of reinsurance. We place reinsurance, and we accept it. One trouble in the American market is that the necessary reinsurance facilities are not really adequate. We have to go abroad; and as a matter of fact there have been proposals in congress from time to time to provide a federal fund to make reinsurance available through American facilities. But the object of that is not to realize any gain, in the main, from the reinsurance operation. The object is to spread the risk, to prevent the catastrophe happening that would weaken the protection.

BY THE CHAIRMAN:

Q. You avoid the sin of profit? A. I do not regard profit as a sin at all; do not misunderstand me there. Our economy is based on profit. It is not entirely a money profit. There is the profit of satisfactory service, and there are other ways under our free enterprise system in which you can enjoy profit other than a monetary profit or a profit in the sense of a gain from an investment which is put out purely for the purpose of profit. I understand all that, but I want to show that for the purposes of this

inquiry you may regard us as operating in every way as an insurance company would be reasonably expected to operate, but we are operating solely for the policyholders, the primary object being the protection, and the other results are incidental attributes that are fundamental, that are just as natural as breathing, in the operations of a modern insurance company. We advertise; we do all of these things, and I want that thoroughly understood.

BY MR. HAYDEN:

Q. Then, Mr. Gruhn, on the question of investment income, I wonder if you would tell me whether the matter of interest and rentals received from investments, so far as the American Mutual Alliance group is concerned, is a major or an incidental matter, so far as these companies are concerned?

A. Well, it is incidental, as I have tried, perhaps unsuccessfully, to explain; in that when you are required to have reserves -- and our statutes in the United States require them -- you invest them.

BY THE CHAIRMAN:

Q. You would be delinquent if you did not make that money earn money; that is the answer? A. Correct; and that is an incidental attribute to the business and represents a small amount in relation to the receipts from investments as compared to the premiums earned, for example.

MR. HAYDEN: I have a statement here which I propose to file.

BY THE CHAIRMAN:

Q. Is that peculiar to this particular Alliance?

A. No.

Q. You heard the factory mutuals yesterday?

A. Yes.

MR. HAYDEN: They said their investment income was a large item.

THE WITNESS: It varies, naturally, as between companies; it varies, naturally, as between groups. Those companies wherein the policyholders make a smaller initial contribution have lesser funds to invest, and the returns are likewise smaller.

MR. HAYDEN: I have a statement here which I propose to file, which in relation to the thirteen companies whom I represent shows, for the year 1943, the gross premiums earned and the gross interest dividends and rent received by these companies, not in Canada only but their total. Then it shows the percentage relationship of that, shall we call it, investment income to the gross premiums received. The figure of relationship is 3.4 per cent. That is the percentage relationship of the investment income to gross premium income. Those are gross figures.

Q. If you wanted to get a net figure, Mr. Gruhn, to take care of investment expense, and to take care of expenses in connection with rental income, it might be reduced to three per cent; is that right?

A. It would undoubtedly be reduced; but when negotiating with taxing authorities and trying to come to some agreement as to what is investment expense and so on, you have an argument; so we have the gross figure there.

MR. HAYDEN: I suggest, Mr. Chairman, that if you wanted to relate this statement to Canadian operations the simple way of doing it would be to take the Canadian premium income, which is shown in the brief and which, for 1943, would be \$2,900,000 odd, and if you apply the three per cent factor, which is the relationship of investment income, it would give you a figure of approximately \$90,000 of investment income, which might be related to Canadian operation on this percentage basis for 1943. May I file these five statements.

Q. Then do any of the American Alliance companies have stockholders and capital represented by shares?

A. No.

Q. You have stock companies in the United States in the insurance business which issue participating policies, though, have you not?

A. Yes.

Q. And I think section 204 of the internal revenue code provides that to the extent of the participating business the companies are permitted to deduct the return or dividends to those policyholders before arriving at their taxable income. Is that right?

A. That is correct.

Q. Then this may seem trite, but I think there is a purpose to be served in the question. Where does the money come from to pay the losses and so on in a mutual insurance operation?

A. It comes from the policyholder; and the policyholder, at the time he becomes a member of the company, makes his contribution, whether it is on a one-year or three-year or five-year basis, depending upon the terms of the arrangement. He makes his contribution in accordance with the rate which is developed for the particular hazard against which he has to insure. The entire operations are conducted out of this monetary contribution of all the policyholders, which creates this common fund out of which all losses and expenses are paid and, as I said, he creates the fund no matter what kind of insurance service organization runs the service, because it is out of his contributions that all the operations of the company are conducted. The investment of the stockholders in the stock company is not used for salaries; it is not used for typewriters and all that sort of thing, as equity capital in a normal corporation is used for raw material, wages, plant and equipment. It is there ordinarily not to be touched

unless the company has bad experience either due to bad management or bad experience because of unfortunate losses. Then when the capital is impaired, if it is not made up; if it falls below the requirements of the statute, the company goes out of business.

The mutual company operates entirely out of funds provided by the policyholders or created by the policyholders, with such incidental income as comes from the handling of those funds and from the normal insurance transactions which the enterprise is set up to perform.

THE CHAIRMAN: I think this would be a good point at which to adjourn.

At 12.30 p.m. the commission adjourned, to meet again at 2.15 p.m.

Ottawa, Ontario,
Wednesday,
April 18, 1945.

The Commission resumed at 2.15 p.m.

Examination of Mr. A. V. Gruhn, continued

BY MR. HAYDEN:

Q. In the operation of these mutual insurance companies do you maintain individual accounts in the sense in which we have heard them described earlier by other parties? A. No, we do not. The insurance operation, generally, is a working of the law of averages as the insurance fund is a fund for the insuring of all classes of policy holders, and you do not concentrate on one special class. In the small arena of particularly large risks the individual account method does not lend itself to the operation. In the first place you have so many small premiums that the maintenance of a system of that kind would be wiped out with expense which was not commensurate with the cost. After all, you try to base the policy holder's contribution in a position where it has a reasonable relationship to the hazard; and when he makes that contribution it, along with others of policy holders similarly situated, creates the fund out of which losses and expenses are paid.

BY THE CHAIRMAN:

Q. That is a reason of convenience, is it not?
A. It is more than a reason of convenience. It is practically a necessity in connection with insurance operations over wide areas and for many policy holders--large, small and medium--and in different hazard classifications. Setting up individual accounts you cannot close the books as of any given date.

Q. Perhaps it would be desirable if it were not so difficult to do? A. Ideally, yes.

Q. Ideally. A. Yes, under an extreme condition. If you could do it in the nut and bolt business, or something like that, it would be a fine thing. But, as a practical matter, there may be fires in connection with a number of risks, and you do not get the report until a week or two, and possibly three weeks later. Therefore you cannot at any given time give a man what he has put in, less what has been paid out on his account, or any other account, so as to be sure that that is the situation at any given time. And it is no more proper to say that when a policy holder has paid a little more, when that little addition goes to a fund that is not paid out in profit, or available to be paid out in profit, but still belongs to the stream of business for the purpose of paying loss, any more than it is to say that when all those policy holders who have had no loss, or those policy holders who have had loss and therefore whose accounts are balanced, would show that the company had paid them any more than they had contributed -- that that extra payment is a profit to those policy holders who are fortunate enough to be paid their loss, or unfortunate enough to have had a loss.

A question has been asked which has caused a good deal of argument and has shown considerable difference of opinion, and that is as to whether we were operating at cost. I maintain we are operating at cost. If you tried to operate a small insurance company with the laws as they are, with policy holder demands as they are, and expectations of the public as they are, it would just be impossible to operate on the actual dollars and cents

individual account basis at any given time.

Q. Or, to put it in another way, it is impossible to estimate the cost of insurance? A. Yes, you are dealing with an uncertain factor, namely unfortunate circumstances. So that if you had it on an individual account basis, and someone precipitated a run, and most of the individual account holders withdrew, you would leave the others who entered into the same contract mutually to assure the loss in a position where they were holding the bag of unpaid losses, because somebody had created a run on insurance companies similar to a run which can be created in respect of banks.

So that to say that in order to have mutuality in a non-profit operation you must have a situation where at the end of a given period when a policy holder quits he must have everything balanced to the cent, is to advocate an ideal situation; but it represents failure to the company. I say that because on that basis there could be no non-profit mutual insurance operation; it simply is not possible.

BY MR. HAYDEN:

Q. This morning we were discussing profit and its meaning. If you take the operations of these mutual insurance companies, and if as a result of good management and favourable experience in loss you have a surplus over your contributions, and everything that has been paid out, and your surplus, why would you say that, for instance, an amount which in those circumstances you would pay to your policy holders would not be profit? A. Are you talking about the difference in the amount that is held over?

Q. Let us take the amount that is held over and the

amount that is paid out. The amount that is paid out in dividends represents, to some extent, a surplus in contribution over your costs and expenses and loss, and then secondly take the amount that is held back. If you can treat them together, all right; and if you can treat them separately, do so. A. That goes to the proposition that even in a mutual company--and I assume that the theory must apply, if the legislation is to be followed, to life insurance as well as to other forms of mutual insurance--that comes to what are termed underwriting gains, or the difference between loss and expense at any one time, which represents profit. Well, it just simply is not logical to say that it is profit in the hands of a mutual insurance company, because it belongs to and goes back to, eventually, those who paid it in. In other words, it goes back to the policy holder members.

It may be an economic gain to someone to buy something for less than his neighbour, but it does not necessarily follow that that economic gain represents either income or profit in the sense set out in income tax statutes. It does not necessarily mean that.

Or, speaking in terms of economics, may I say that I have a man who comes to my house once a week and cuts the grass and does the work around the house. I should be doing that work, if I stayed at home. However, I have to come to Canada, and have to go to other places on occasions such as this. So I pay that man. If I did the job myself, and saved that money, that would be an economic gain to me. It is not income or profit.

Q. In other words, it is a saving. A. Yes, it is a saving. And when a policy holder makes that same contribution in a stock company, I want to emphasize the

fact that, with the exception of the unearned premium reserve, the ownership of that money passes from the policy holder member to the stockholder shareholder. He is the one who determines what shall be done with it -- whether it shall be paid out in dividends, or whether it shall be held, or whether it is needed or not to meet some tax statute. The ownership passes, and that is why it becomes profit in the hands of a third party shareholder. It cannot logically be profit in the hands of the person who contributed it in a mutual company, because it is not contributed for the purpose of making profit. It is contributed for the purpose of furnishing protection for himself and for others similarly situated.

BY THE CHAIRMAN:

Q. After all, it comes down to this, does it not, that a sum of money earns income. In the hands of a mutual company, as in the hands of a stock company, that is true, is it not? A. Yes, certainly.

Q. In the sense that it is capital in both cases. A. No.

Q. I am thinking of the investment yield. What is the difference between a sum of money in the hands of mutual insurance companies and in the hands of stock companies? A. Do you mean receipts from the investment of funds?

Q. I am speaking of investment income. What is the difference in the two forms? A. In connection with investments, in the case of the stock company, when a policy holder's funds, which are no longer his--except as to the unearned premium--are invested, they bring in a return that goes to the shareholder.

Q. But it is funnelled through the hands of a

distinct legal corporation? A. That is correct.

Q. A corporate body. A. Yes, that is correct. Now, in the mutual company those same funds are invested, and they bring in a return or a receipt to the company. That is an economic gain or a saving to the policy holders, whichever way you wish to look at it. If you regard it as an economic gain, it is a gain even in the sense that the operation is a non-profit operation. But it is, incidentally, a gain, and it may be first regarded as having been used to pay losses -- but nevertheless it is an economic gain because it reduces the amount of the policy holders' contribution.

This may be getting a little ahead of the story. The reason for the tax plan, as it finally developed in the Congress of the United States -- and the program of taxation which was finally passed was that of taxing mutual companies on their investment income solely, or one per cent of the gross receipts, whichever were the greater -- was predicated upon the theory of certain experts before the committee on finance and the committee on ways and means who, after making a study of the proposition, concluded that there was no profit element in the mutual insurance set-up at all, other than the possibility in connection with investment income.

Q. Mr. Freeman told us yesterday that they could not put their finger on the profit and therefore they did not tax it. A. They hold two theories in respect of non-profit organizations. Even in state charitable organizations, or mutual benefit associations, or life insurance companies, or mutual ditch and irrigation companies-- whatever it may be--if the members' moneys are rented out, so to speak, and there is a return on that, they

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Mr. Gruhn

hold that for taxation purposes, and particularly in war time, there is an element of gain there that probably was properly taxable.

Q. That is so in the case in England. A. I believe that is so.

Q. The golf club case. A. That might be an economic gain to the world, if all golf club memberships were taxed. It would help me a great deal.

But may I point out that from 1918 to 1942, in the consideration of the taxable status or the probable taxable status of mutual insurance organizations in our federal set-up, that by ruling the established policy of the Bureau of Internal Revenue the investment income in a mutual company was first considered for accounting purposes as having been used to pay losses, and then expenses. But as I say, the application of that is unnecessary, in fact, under this tax law, because the investment income is taxed at the going rate, and on the theory which I have indicated.

Q. It is not paid out of investment income; you pay it out of the deposit, do you not? So that it is as broad as it is long? A. You do not take investment income and stick it into your vest pocket, and premium income and stick it into your back pocket, and some other income and stick it into your side pocket, and then when you have a loss or an expense just scratch your head and decide which one you are going to use, or which pocket you will reach into. It is, again, an application of the law of averages.

Q. But it might be good accounting to do so, though. A. From the standpoint of accounting, it is done. But you do not need to maintain a series of pigeonholes for

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Mr. Gruhn

your funds, and pull one out, or the other. But I wish to emphasize, incidentally, because of the allegations on the part of those would will it that way, -- and again I am not splitting hairs over the choice of a word -- but the suggestion is made that that incidental element of profit makes the entire venture a profit making venture. As a matter of fact, it is not any such thing.

BY MR. ARNASON:

Q. Did I understand you to say that investment income with respect to mutual companies tends to reduce the cost of insurance to the policy holders as compared with the increased return on investment to stockholders in a joint stock company? A. Yes, that is substantially correct.

BY MR. VAUGHAN:

Q. When a subscriber withdraws ---

MR. HAYDEN: There is no subscriber here; it is only a policy holder. You mean a member.

BY MR. VAUGHAN:

Q. When a member withdraws, or says, "I do not want insurance, and I will withdraw from the organization," how does he participate in the reserve? A. He does not participate in the reserve, except in the case of a dissolution; and I am not talking in terms of disaster. I am talking of the mutual corporation as a living organism which continues indefinitely -- because we have over sixty companies in the United States well over one hundred years old. However he may have got more out of the pool than he paid in, and he may have got a trifle less. It all depends upon the period of his getting out, at the time he decided that he did not want mutually to insure with the others any longer.

As I have tried to explain--and I am sure I have not

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made myself clear--we have no individual accounts for the policy holders. It is an average proposition. It is insurance in its fundamental sense, the sharing of the losses of the few by the many. And there is no absolute exact accounting for each member at any particular time; over a period of years it washes out, and washes out most equitably, when you allow the law of averages to apply.

Q. If a member has no right to the reserve, or to share in the reserve, you say that that reserve is an association reserve rather than a member reserve.

A. It is the members all taken together. It is all taken together. What is held over is held for three reasons: first, the laws of the state say that as a prerequisite of licence, whether or not it is a non-profit corporation, a mutual company shall have a surplus of so much money. For example, in New York it runs well over a million dollars. Now, when you have a lot of insurance in force you create an amount of risk that is very very large, and you are dealing with uncertainties. You have outstanding a great many potential obligations. Members are interested in security, and they want protection that that security affords. Therefore, as the amount of risk increases, it is necessary to increase the reserve and surplus even beyond the minimum required by statute. The third factor is the tempo of the competition as set by those who do the bulk of the business. They have educated the public to believe that only in size lies strength.

The small contribution was the subject of considerable discussion back and forth yesterday, as to whether policy holders upon leaving the company for any reasons, received an exact accounting in dollars and cents showing loss,

expenses, investment income and so on, and there was discussion as to whether that element represented a profit to the company. Well, it cannot represent a profit to the company, because it is not paid to anybody. It still is the fund that is necessary because of the law, and because of the needs of the policy holders with which he combined to secure protection. It is still there, available for the losses which may have occurred on the very day he got out, and must be paid within the ensuing time.

BY MR. HAYDEN:

Q. In Appendix No. 4, a recapitulation which appears in the brief, we show figures of the balance, or what might be described as the hold-back for the period of fifteen years, from 1929 to 1943, and that figure is 2 per cent of the net premium. It amounts to \$776,910. Then, if you examine the return of those thirteen companies for 1944 to the Department of Insurance--they have not been assessed and published yet--you will see that that figure of \$776,910, representing the accumulated hold-back over a period of fifteen years is eaten into in 1944, so far as the Canadian business of these companies is concerned, to the extent of \$530,482. So that if this recapitulation had been carried to 1944, instead of showing a figure of a hold-back of 2 per cent and \$776,910, it would be approximately \$250,000, or something less than one per cent.

That is the purpose for which these reserves are paid. The policy holder, when he is in there, gets the benefit by reason of his contribution; and when he steps out the purpose still has to be maintained. There is an illustration; we might say it is a profit today, but who can say that by December 31, 1943, it was a profit. Some

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of those losses may have been on the way.

MR. VAUGHAN: Still, there comes a point when you know there is probably more reserve than is necessary, does there not?

MR. HAYDEN: The question then is whether something less than one per cent of the net premium is or is not sufficient reserve. That is the situation at the end of 1944.

MR. VAUGHAN: One can understand the wisdom of a statutory reserve, and even a voluntary reserve on the part of an association, as a matter of protection. But I took it this morning that there was a revenue or an income of \$90,000 from investment; is that correct?

MR. HAYDEN: Yes.

MR. VAUGHAN: Calculated on the proportionate basis.

MR. HAYDEN: Yes, that is correct.

MR. VAUGHAN: That represents a pretty big income.

MR. HAYDEN: In relation to the volume of business; in 1943 the net premiums paid were \$2,900,000. If you take it in relation to the risk you get into a very large figure -- the value of properties insured, I mean.

MR. VAUGHAN: To get back to the first point, what was in my mind was that if the members were not entitled to share in the reserve, then does not the reserve belong to the association rather than to the members?

MR. HAYDEN: Well, maybe again we should cut through, because I said in opening yesterday that because it is a corporation that does not make anything that it does or any income that it gets taxable income. We have to go further than that. I say it belongs to the members. It may belong to the corporation; but what is the corporation?--because everything of the corporation belongs to

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the members.

MR. VAUGHAN: Theoretically; but we are told the members do not get it, and they have not any right to it.

THE WITNESS: The members do get it.

MR. HAYDEN: They do not get it handed out to them, because we do not operate that way; but on liquidation they would get it.

MR. VAUGHAN: On retirement they do not get it.

MR. HAYDEN: No, because we do not operate on an individual account basis. We are still a mutual insurance company, selling mutual insurance.

THE WITNESS: May I interject here that I do not think it was understood that it is a requirement in the United States that surpluses be maintained. And that is a requirement which has to be met, or you cannot function as a mutual company. If that accumulation which counsel has spoken of had been taxed at 40 per cent on the assumption that it was profit, as \$500,000, over the fifteen year period, and assuming that 40 per cent would be \$200,000 for tax purposes, on the assumption that it was profit, and then you come along to 1944, in Canada, where the mutual operations suffered substantial loss, those very same funds which were paid in or contributed by policy holders would have carried the burden of a profit tax of \$200,000, when there was no profit. Because in the over-all operations of the years there was close to being a loss. And that would have been a charge on the policy holders, the members in the group who made the contribution. That would have been a charge on them as a profit; and in no sense, in terms of a properly taxable profit, was it a profit.

BY MR. VAUGHAN:

Q. Does not the joint stock company have that same condition to contend with, to determine its results? They have losses which may be current, or which may happen before the end of the year? A. That is true, yes. But if it is a weakness in the tax structure of joint stock companies, or capital stock companies, as they like to be called in the United States--and when I talk about stock companies I am talking about United States companies, because they are practically the same companies which are doing business here--they are not concentrating on correcting the weaknesses in their tax structure, if there be any; they are solely interested in placing an arbitrary, improper and unnecessary burden upon mutual companies, without regard to the policy holder or the public interest. I do not know whether it is a weakness or not in the taxation of a profit-making concern. But they are, frankly, in business for profit. They should not be ashamed of it, and they ought to recognize that, of necessity, there is a natural differential in the treatment of a non-profit corporation from that accorded a profit corporation. I do not think it is any good for United States companies to come to Canada and cry about it.

BY MR. HAYDEN:

Q. Now, while we are on this subject, it seems to me it might be appropriate to bring in a question I had intended to ask. You were telling us that the same joint stock companies operate in Canada and in the United States. Now then, in the United States when these questions were before Congress, as to the taxation of mutual companies, were the representations made by the stock

MEMORANDUM

The following information was obtained from a review of the records of the Department of the Interior, Bureau of Land Management, regarding the land owned by the United States in the State of California.

The total area of land owned by the United States in California is approximately 100,000,000 acres. This land is divided into several categories, including National Forests, National Monuments, and National Antiquities.

The National Forests are managed by the United States Forest Service, which is a part of the Department of the Interior. The National Monuments are managed by the Bureau of Land Management, which is also a part of the Department of the Interior. The National Antiquities are managed by the National Park Service, which is a part of the Department of the Interior.

The land owned by the United States in California is primarily located in the western part of the State. The largest areas of land are located in the Sierra Nevada Mountains, the Coast Range, and the Sierra de las Uvas.

The land owned by the United States in California is primarily used for recreation, conservation, and agriculture. The National Forests are used for recreation and conservation. The National Monuments are used for conservation. The National Antiquities are used for conservation and agriculture.

The land owned by the United States in California is a valuable resource. It provides a source of recreation, conservation, and agriculture. It also provides a source of income for the State of California.

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companies the same as we have heard today -- that is, the question of unfair competition and discrimination?

A. Yes. All of the general allegations, charges and statements were advanced in the United States over a long period of years, and are continuing to be advanced.

Q. Have you been able to find anything reflected in the operations and balance sheet position, and the profit factor, of the joint stock companies which made those representations of unfair competition and discrimination that would support any allegation to the effect that there had been inroads into their business? A. I cannot find where they have been hurt a particle. As a matter of fact, when you look at their business done, you find that it has been constantly increasing.

Then, when you look at their profits and dividends to stockholders, on capital actually invested--cash on the line invested by stockholders--might I say that we have taken a list of the United States stock companies doing business in Canada, and I think it is pertinent to this inquiry, due to the complaint that they are being hurt, that something further be said on the point. When the claim is made that they are unfairly discriminated against and hurt, and that they must be adversely affected, it seems fair to take a look at the dividends. That will take only a minute. I shall give the names of the companies and the insurance dividend on the basis of capital actually invested for 1943 and for the ten-year average including 1943.

Q. What is the source of your information?

A. The source of the information is that gained from checking and perusing Best's Insurance Reports,

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Spectator reports, and the other standard insurance reports which carry this essential information in respect of all companies.

Q. You are referring to **fire** companies? A. Yes.

Q. I have a statement which I might file.

A. These are the percentages of dividends paid, related to the capital actually invested in cash on the line by the shareholder. It does not include stock dividends, but it includes cash laid out on the line by the stockholder.

BY MR. MANN:

Q. It has no relation to the surplus? A. It has relationship to the investment. These are the figures:

	On Basis of Cash Invested - % Dividend	
	<u>1943</u>	<u>10 years</u>
Aetna Insurance Company	22.7	21.6
American Insurance Company of New Jersey	8.6	8.2
Continental Insurance Company	61.6	54.7
Fidelity Phoenix Fire	26.6	21.9
Firemen's Fund	9.9	7.8
Glen Falls	12.8	11.3
Great American	6.7	8.3
Hanover Fire Insurance Company	5.4	6.3
Hartford Fire	7.1	15.7
Home Insurance Company	13.3	12.8
Insurance Company of North America	13.9	14.6
National Fire, Connecticut	5.2	5.2
Niagara Fire	18.0	17.4
North River	17.1	16.7

$\frac{1}{n} \sum_{i=1}^n x_i = \bar{x}$

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Phoenix Insurance, Connecticut	30.0	27.0
Queen Insurance Company	53.3	67.7
St. Paul Fire	106.7	87.5
Springfield F and M	47.5	47.0
Travellers Fire	3.8	2.8
United States Fire	27.2	26.9

Now, so that some people may not turn cartwheels, let me make an explanation. I shall take as an example the St. Paul Fire and Marine Company, a United States company. I believe this shows justification for a substantial difference in treatment between the mutual company and the stock company. I would point out that the total cash actually invested by stockholders was \$1,500,000. The total policy holder surplus, including this cash capital, and \$8,500,000 stock dividend, is \$36,760,595. The resources of that company are made up almost wholly out of the contributions of the policy holder. Third party interests invested in cash, \$1,500,000.

BY THE CHAIRMAN:

Q. Is that wholly a fire company? A. Yes, it is a fire company.

Q. Any marine business? A. I do not know. I do not know whether it has any ocean marine, or not. It may, to some extent, be in the inland marine field, but what I say on that would be subject to correction.

So that, in 1943, on the basis of the \$1,500,000 which the stockholders put in, they got a return in one year of \$1,600,000. The average return from 1931 to 1943, in each year, was \$1,230,769; and since organization the cash dividends were \$26,548,694.

That is an average, on the basis of cash invested,

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of 106 per cent for 1943. Now, I wish to be absolutely fair about this, and I shall say that on the basis of policy holders' surplus, which the stockholders own, but which is the policy holders' contribution, the return is 4.4 per cent for 1943, and for the ten years it is 3.3 per cent.

I can say this of the United States companies, that I am almost moved to tears over the sad tax plight of those policy holders, under those conditions. They may need relief -- but I do not know what kind of relief it is. I think they ought to take great pride, and the management of those companies ought to take great pride in the fact that they have so successfully conducted the business of fire insurance, for the profits of the stockholders. They have rendered a service, true, to the policy holders. But I submit that, from the profit standpoint, from the standpoint of the stockholders, they ought to be here, admitting that "we are making substantial profits; we are not hurt, but we do not like any kind of competition, especially if it is non-profit, and we think that we ought to gain the advantages of the investing of the entire insuring public's premium contribution."

I do not think they have a case, on the basis of being hurt. And so far as I am concerned I shall always contend--and I do so on the basis of an economic philosophy which I think is sound--that no matter what the tax system is, there must in fairness be a substantial difference in the tax treatment of a profit-making company, operated for the benefit of third party interests, and a company which is an organization for the protection of policy holders, and operated solely for the

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policy holders interested, and in the interest of those policy holders. It seems to me that is only logical and fair.

BY MR. HAYDEN:

Q. A similar statement was made for the casualty companies. A. I shall not take time to read it.

MR. HAYDEN: I shall file this statement.

BY MR. VAUGHAN:

Q. You said you wished to be fair in this statement. Do you think these percentages are fair, when the reserves which are set up and which are held in the company as reserve are not taken into account? Do you think that is fair? A. I have given stockholder dividends, and I am taking it from the standpoint ---

Q. Of the original capital put in? A. Yes.

Q. But the shareholders have been allowed a certain amount of profit for probably one hundred years.

A. They have allowed profits to accumulate, it is true, in that the St. Paul Fire and Marine has a stock dividend account of \$8,500,000. That was profits they left in the company. So that the stockholders' capital contribution in that sense is \$10,000,000. But, the point I make is that in a profit making insurance business you reap the benefit of large contributions with less hazard than you do in an industrial enterprise because -- an economist may disagree with me, and certainly the stock companies will disagree with me when I say that when you invest in a stock company, in a normally successful operation, there is almost a double investment, in that inasmuch as the money is not used in buying equipment and that sort of thing, as it is in an industrial enterprise, or a big merchandising enterprise, yet it is

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reinvested and there is a double return on it, in a sense. That may be straining the point a little bit, I will admit, but I make the point on the basis of the cash invested. The investors have not done at all badly -- and I wish, by the way, that I had some of the stock in the St. Paul Marine and Fire Company.

BY MR. HAYDEN:

Q. Let us consider mutual dividends to commercial policy holders. There was some discussion about the matter, and some question as to whether or not it produces a substantial tax to the government. What do you say about it? A. Yes, it does. There again I will get into a quarrel, I suppose, with the stock companies. I do not know whether to call them my friends or my enemies; I never have been certain. In most cases in the United States they are my friends. The situation is this: we made a calculation when the tax fight was on in Congress, on this basis, that we made tests--we did not get reports from every policy holder--but so far as our United States operations are concerned, and I believe this will probably hold true of Canada, although possibly not to the same extent, about 70 per cent of the premiums came from the type of policy holder who could take his premium payments as a deduction, as an insurance expense, in the computation of his tax return. If that premium payment was \$10,000, he had \$10,000 as a deduction, or as an expense item, before computing his net income subject to taxation. That is true, whether that \$10,000 is paid into a stock company, or into a mutual company.

Then, take the mutual company: let us assume that

it returned 20 per cent of that. That 20 per cent of \$10,000, or \$2,000, goes into the **next return as income**, and increases his income by \$2,000, producing that much more tax. Now, taking off, or making some subtractions to allow for certain equations, that would have produced, at the rate in the years in which the calculation was made--and it was made before the larger rates were imposed on United States taxpayers--it would have on that theory produced a tax of \$18,000,000. That compared favourably with the amount of taxes in that period paid by the stock insurance companies, or the profit-making stock insurance companies, to the federal government.

I feel great confidence in advancing that consideration to you, because I have but to quote from a photostat of insurance cost and taxation, a document distributed by Bethea and James, who represent **a large group** of stock insurance agents in the United States. The agents are calling this to the attention of mutual policy holders, or prospective mutual policy holders. I shall not read it all, but I think it is very important, as bearing out the proposition I have just laid down. This is what the document states:

"Let us assume that a successful corporation, one making a substantial profit each year, --"

And this is talking about a policy holder --

"---is hesitating between mutual and stock insurance. The Mutual Company offers a 20 per cent dividend and the corporation buyer is debating whether or not the 20 per cent saving would justify his taking a chance and joining a mutual company. At this point the stock agent should ask the buyer to consider the corporation's earnings and taxation. On the net

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premiums may be charged off as a business expense and, therefore, the corporation must pay taxes on the amount saved by purchasing the lower cost insurance.

"If the buyer is in the income brackets where 40 per cent, 50 per cent or 60 per cent of its earnings go to the government, then 40 per cent, 50 per cent or 60 per cent of the mutual saving will go to the government. In such a case, the difference in price between mutual and stock insurance is not 20 per cent, but 12 per cent, 10 per cent or 8 per cent depending upon the tax bracket. This means that in such instances the insurance buyer may for a relatively small difference in price secure all of the advantages that go with capital stock insurance-- the highest security, agency service and the satisfaction of supporting the profit system.

"The demonstration of these data can be of extreme importance in a close case. If it is possible for the agent to ascertain the corporation's earnings, he can present the figures himself. In the event, however, it is not possible to learn the taxable income of the corporation, he can still present the argument to the buyer, and it will still have its tremendous effect when the buyer has worked out the proper price differential for his own information."

There is their own answer to the mutual competition, and they have got it figured down to the point where it is all in their favour. They have told those who were responsible for placing this on the agenda as an item for consideration by a royal commission, that they were badly handicapped in competition and needed relief under the tax laws, in order to save them from -- well,

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I do not know from what.

BY THE CHAIRMAN:

Q. What do you regard as a chance? The writer suggests that the insured would be taking a chance in joining a mutual. These are the words, "would justify his taking a chance and joining a mutual company"; what is that chance? A. You have got to be familiar with the other side of this propaganda campaign directed against us. To the United States government and the Royal Commission they say that the mutual companies are huge profit-making concerns piling up huge surpluses that belong to the policy holder, and that that represents profit which ought to be taxed. To the buyer of insurance they say -- and again, if you will permit me, I shall file with the Commission copies of propaganda extending back for almost a hundred years -- they say to the prospective buyer, "if you insure with a mutual company you take a big chance. It has no capital structure. There is nothing upon which you can rely for the loss which will occur when the going gets rough. You are liable for all you own if you insure in a mutual company." I am almost quoting verbatim.

BY MR. HAYDEN:

Q. The question was raised in connection with rate loading. I understand that in the United States your rate carries specific loading for income and excess profit taxes. A. Our fire companies and our casualty companies are members or subscribers to many rating organizations, and in no case do I know of a loading being incorporated in the rates. These rating organizations serve stock and mutual companies. There is, particularly in the case of casualty insurance companies,

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a loading for taxes which represents the premium taxes payable to the state. That is ascertainable through the item of expense, and there is a loading in the rate for that. If there is no actual loading in the rate for income and excess profit taxes, from the figures which I have read you can tell why there cannot be, because it depends upon how the company comes out at the end of the year, as to whether it has made a profit or not. And if it has made a profit it pays a tax. If the shareholders, who invested money for the purpose of making money, have made that money, they pay a tax. If they have not made money they do not pay a tax. However, I do not wish to get into the realm of economics, and argue as to whether or not eventually the consumer pays all taxes. There are economists who hold, and a prominent economist writing for one of our American syndicates points out, that the argument that there is double taxation in a profit-making corporation when you tax profits in the hands of a corporation and also in the hands of the stockholder, that that argument goes completely out of the window when you contend that the consumer pays all the taxes. Because if he does, it is not a double tax on the shareholder of the corporation; rather, it is a double burden on the consumer.

Q. Be that as it may; in your opinion is it the policy holder or the shareholder who bears the burden?

A. In my opinion, the way the rate structure is set up, it is the shareholder who pays, and who should pay.

Q. Tell me, then, is the mutual dividend of a policy holder taxed in the hands of the member? A. If you impose this proposition -- and this proposal is to tax mutual companies on the same basis as stock companies --

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the policy holder surely pays it. I wish to add this, that in the United States this proposal has been made ever since 1918, namely that the government in some way or another has been asked to consider taxing, either by interpretation of the existing law or by the passage of new law, mutual companies on the same basis as stock companies. That fact was particularly argued in 1928 and 1929. It was before Congress in 1932, before the Senate Committee on Finance in 1937 and 1938, before the Committee on Finance in 1941, and before the same committee in 1942. And every time it has been knocked into a cocked hat.

Then they come out in war time with a proposition which I have explained to you -- a tax on investment income solely, or one per cent of the gross income, which includes premium income and investment income, less certain deductions. And that is comparable to the situation we have today in Canada. We are paying the difference between the two, which would go to the provinces; and the one of the three which we are paying represents substantially the tax which the mutual companies are paying to the federal government in the United States. And that is the only tax they are paying.

Q. I understand your companies pay on the gross income basis, do they, in the United States? A. In the main, it works out, for most companies, on the one per cent basis.

Q. The one per cent basis, you say? A. Yes.

Q. And, a last question: you have already told me, but I may have missed it -- as to how United States authorities treated the receipts from investments.

A. In the statement I made I have already explained that. They have treated it as an ordinary proposition.

BY MR. ARNASON:

Q. Mr. Gruhn, could you give us some information as to the average size of the insurance risk written by your Canadian companies? A. I am sorry I do not have the information, but I shall be very glad to ask the companies for it.

Q. That is not necessary. A. I would be very glad to do it if they have the figures worked out on that basis.

BY MR. BROSSARD:

Q. With the permission of the Commission I should like to restrict my examination to as few questions as possible, leaving it to my learned friends Mr. Mann and Mr. Geoffrion and others if they care, with leave of the Commission, to further cross-examine. I understood you to say, Mr. Gruhn, that the American Mutual Alliance was composed of three constituent organizations? A. That is right.

Q. Which themselves are not incorporated? A. The three associations are incorporated, non-profit, business leagues, under the laws of the state of Illinois. The Alliance is unincorporated.

Q. And the thirteen companies which you represent to-day belong to one of those three constituent organizations? A. One or the other, or maybe two of them.

Q. Possibly two. In what manner does the Mutual Alliance purport to speak on behalf of the individual companies? A. We speak on questions such as this where two or more companies are affected. If it is a matter of general public concern we speak for them. Any time any commission or any state authority wishes the appearance of an individual company official, that appearance is gladly arranged for.

Q. May I ask whether in this particular instance the thirteen interested companies have had an opportunity to

see your brief and approve of it? A. The counsel's brief has been sent by our office not only to the thirteen companies, but to all the companies in the association.

Q. What proportion of the entire membership of these three organizations do these thirteen companies represent; a small or substantial proportion? A. Oh, they represent the relationship that thirteen bears to about 105.

Q. Would you tell us what type of insurance operations these thirteen companies carry on in Canada? What type of risks do they insure? A. They insure all types of risks, substantially, other than farm. Fire and casualty and dwelling houses and mercantile establishments; manufacturing plants, department stores, banks,

Q. Do they insure automobiles, also? A. Yes, automobile insurance.

Q. What is the type, generally, of the insured which the companies try to secure? A. The high class of citizen which you usually find in Canada.

Q. Is there a particular selection, in other words? We have heard others tell us that they restricted their risks to particular, selected insurance?

A. I will resist the temptation to explore that any further than I should for the purpose of answering your question. All companies, including stock companies, boast of their underwriting sagacity and their concern for the type of wholesome risk, may I put it, that they assume. None of them wants to insure the irresponsible bum, or a person of that kind; but I know of a stock company advertisement which says, "We exercise the utmost underwriting judgment humanly possible."

Q. And I suppose this is the policy followed by your thirteen companies? A. Yes, certainly.

Q. What I had in mind was whether you had large risks only or whether you also insured small risks?

A. Small, large or medium.

Q. Is there a considerable turnover in the membership of the insured? A. There is some. The extent of it, I do not know.

Q. But it varies from year to year, to some considerable extent? A. I would think so.

Q. To some substantial extent? A. I do not know whether it would be regarded as substantial over the long time pull. I would not know whether it was one per cent or two per cent or five per cent.

Q. Are you personally connected with any of these thirteen companies? A. Oh, no. I made that statement earlier.

Q. Could we assume that they operate somewhat on the same basis, the thirteen of them, or on a practically identical basis? A. Oh, yes, in all substantial respects.

Q. In regard to the fixing of premiums, in regard to policies, in regard to the setting aside of reserves and so on? A. Yes, in the main.

Q. And as regards their policy as to the payment of dividends? A. It may vary from company to company, but for the purposes of a matter of this kind, I do not think there is any difference.

MR. HAYDEN: No essential difference.

BY MR. BROSSARD:

Q. How do they go about getting their new members?

A. There are various means. I said this morning that the servicing organization uses all the modern methods that are worth while. They may be represented by agents, who may be compensated either by a commission or by a salary. That in the main is their representation; or they may be

represented by combination representatives, who serve as engineers, similar to the set-up of the factory mutuals, but only similar to a degree.

Q. But substantially they are represented by agents who are remunerated on a commission basis in the same manner that stock insurance companies are represented? A. Yes, certainly.

Q. Do they ask from the new subscriber, or the prospective policyholder, the execution of a formal application form? A. Generally, no.

MR. HAYDEN: There is an application.

THE WITNESS: There is in connection with all automobile insurance, as was pointed out yesterday, where certain facts are required concerning the car, the occupation of the driver and owner of the car, and that sort of thing, but from the standpoint of general operation the answer would be No.

BY MR. BROSSARD:

Q. So the only evidence of the undertaking of the policyholder on the one hand and the company on the other hand is the policy which is issued? A. Yes.

Q. Yesterday you filed -- . A. Counsel filed it yesterday.

Q. Yes, counsel filed a policy of the Lumbermens Mutual Casualty Company, and National Retailers Mutual Insurance Company. A. Yes, and automobile policy.

Q. Can we take it that this policy in its essential conditions is similar to all other policies issued by the other companies? A. Yes. Mutual companies in the United States in the fire insurance field use the standard fire insurance policy. In many states the form of policy is required by law. They use a standard automobile policy; they use uniformly a workman's compensation policy,

and as a matter of fact they are almost identical, outside of the mutual provisions, with the stock company policies.

Q. How is the premium rate established and determined?

A. The mutual company may either make its own classification or it may be a subscriber of a rating bureau. It may have its own rating bureau. There is a variety of methods.

Q. Generally how do those rates compare with the rates of the stock insurance companies? A. They are approximately the same. In many states of the United States they are exactly the same; and in many states of the United States -- I do not know whether or not this is true here -- they have to be, by law. There are uniform rate requirements for all companies. For Virginia, for example, and the District of Columbia, by law all companies are required to use rates which are approved by the supervisory official, in the case of Virginia the corporation commissioner and in the case of the District of Columbia the superintendent of insurance.

Q. Are these rates established by the experience of each company, or are they based on general tables? A. Rates generally in the insurance business are, or should be, based upon general experience. I am perfectly glad to discuss this with you, but I do not want to go into it too deeply. In regard to fire insurance rates, however, that is an involved question; and I will say here very frankly that they are based upon the exercise of what raters call a sixth sense; that is, judgment and experience do not have a great deal to do with it, except in a general way. And that is very properly so, because there are certain immeasurable factors in fire insurance that are measurable in the case of Workmen's Compensation or automobile insurance, for example.

Q. I suppose those immeasurable factors would be included in the margin of safety of which we hear so much?

A. Oh, yes. They have their schedules as to charges and credits. There is a charge of so many cents made for this and a credit for that, and so on. I think some time, and the states are coming to it and I hope the dominion is coming to it, they may have a royal commission to investigate how fire insurance rates are made up.

Q. But on the whole we can assume that your rates compare with the rates of stock companies doing the same type of insurance?

A. That is right.

Q. Now in regard to the rights of the policyholders, I see in this form of contract a general clause which reads in part as follows:

"This is a participating policy under which the Board of Directors may, in its absolute discretion, subject to the charter, by-laws, classifications and resolutions relating thereto, determine and pay unabsorbed premium deposit refunds (dividends) to the insured."

Is this clause the only one in your type of policies which sets out the rights of the policyholders, except such rights as they have to the payment of the compensation in the event of the risk being realized?

A. Such rights are inherent in the nature of the company and on matters of fact under the laws under which the company is incorporated.

Q. What would be the rights of the policy holders under this policy we have here, in regard to a payment of a dividend, on any basis whatever?

A. Naturally when you have any kind of a corporation the members elect their representatives on the board of directors, who manage the corporation. It is the directors who are, or should be, in close contact with the affairs of the corporation; who get all the reports, who elect the officers, who make the studies and make the decisions respecting

company policy, and who determine, when they have the facts before them, what should be done in the interests of those whom they represent, that is the members of the Company. That is true of any corporation; and of necessity matters of this kind have to be left to the direction of those who are charged with the responsibility, because they must know what the situation is and what the requirements of the situation are; what the equities are and what should be done in the interests of the protection which the policyholders, acting in combination, are pledged to give.

Q. But am I right in stating that a policy holder has no right to a share of the, let us say, investment income, or to a share of the reserves other than those which may be decided upon by the directors? A. That is true; and such changes as may be made in the authority of the directors at any meeting.

Q. As a rule are the meetings of shareholders attended by a large number of shareholders, or is it not your own experience -- ? A. The typical American corporation may have its meetings attended by only half a dozen members, but I have known meetings to be attended by as many as a thousand.

Q. In your experience in connection with these particular companies -- . A. When things are going right it is typical that there is not a large attendance. It varies. I know of one officer of one mutual company in upper New York State who goes about telephoning members to come to the annual meeting, reminding them of it, and having difficulty having them to come in, particularly policyholders who have been members for a long time. In my judgment that does not affect the mutual characteristic of the enterprise, or the members' rights, or anything else. I did not vote

last Saturday in my village. That does not affect my rights as a citizen.

BY THE CHAIRMAN:

Q. If they are satisfied they do not go. If they are dissatisfied, they do go? A. I know of the case of one company in Providence years ago where they stormed the doors, they were so angry. Human frailties are to be found even in mutual insurance, I am afraid.

BY MR. BROSSARD:

Q. You have said that there is a certain turn-over in the membership of these companies?

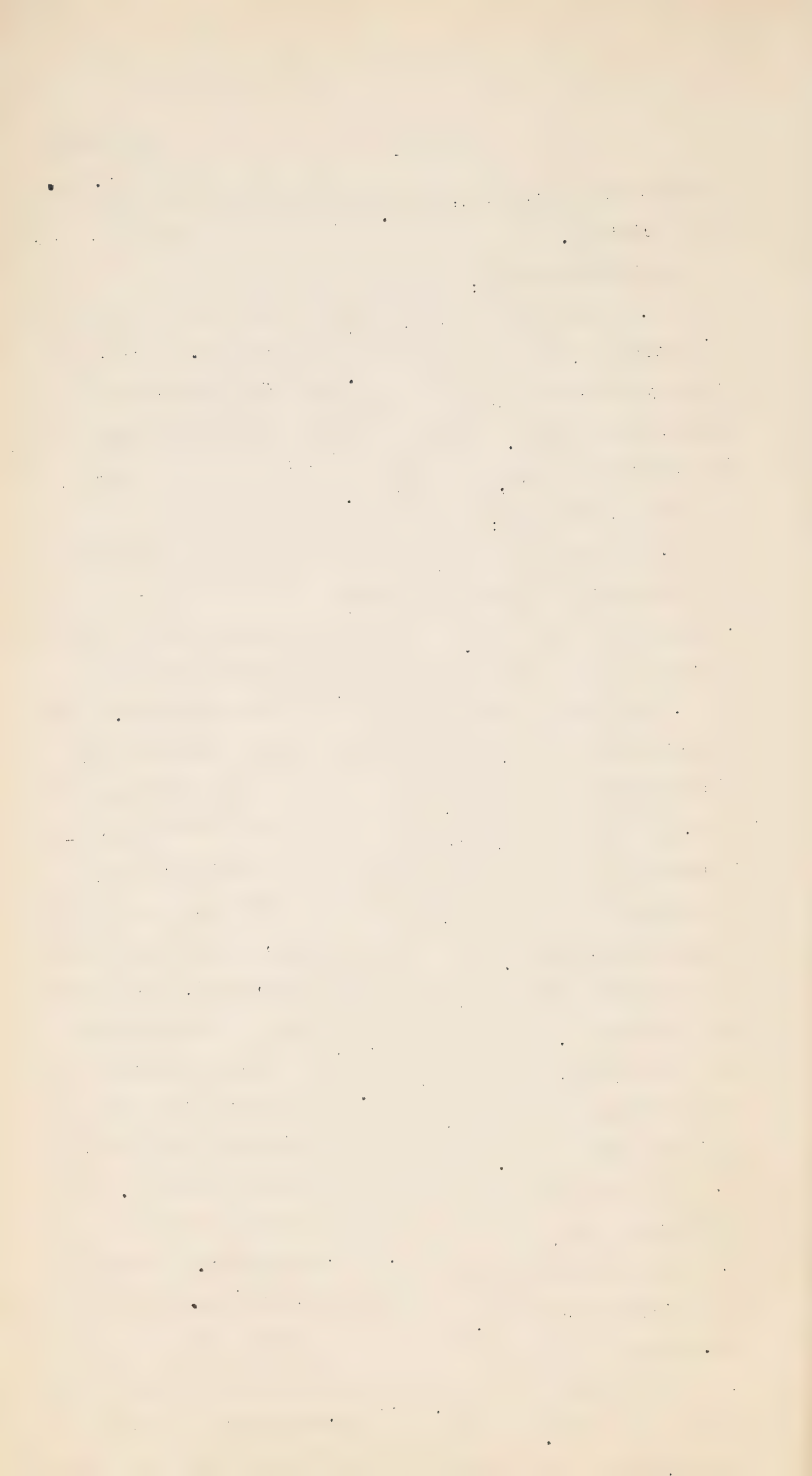
A. There is bound to be. There is pressure on the mutual policyholder to cancel his insurance almost every day.

Q. You were asked by one of the commissioners what was the position of the shareholder who either cancelled his policy or did not renew it, in so far as reserves were concerned, or undivided profits? Could we take the case of a company where a certain number of policyholders have discontinued at the expiration of say 1942, and who no longer remained policyholders. Then on January 2, 1943, a certain number of persons would become policyholders of the company for the first time, and at the expiration of 1943 we will say the company declares a dividend. Do you consider that in that dividend there is a certain proportion of investment income included? A. There may and there may not be.

Q. That proportion of the investment income was gained in the previous year, let us say? A. All right.

Q. The gain was not for the policyholder who ceased to be a policyholder? A. But when he left he got a dividend.

Q. Yes, but not in respect, perhaps, to a share of that particular year? A. I have already explained to the Commissioner, and I stand on my testimony, that some policy-



holders may have obtained, in the way of loss service and dividend, more than they paid in, and some less. It is an average proposition. The exchange between the gentleman here to my right and myself was on that very point, whether a policyholder at any given time got exactly, to the cent, everything he put in. I said No, and I still say No. He may and he may not. It all depends on the circumstances at the time.

Q. I see here in appendix 4, which covers the fifteen years from 1929 to 1943, in the recapitulation sheet the dividends or unabsorbed premiums returned to policyholders; and if I understand it, that is for each company, including the American and Canadian business?

MR. HAYDEN: No, it is only Canadian business.

MR. BROSSARD: Then I will withdraw that question.

Q. Could you let me know whether in any year since 1929 any of these companies has returned by way of unabsorbed premiums amounts in excess of the underwriting gain or profit?

A. That includes the period of the depression, because this is an average proposition; it is real insurance, so it is entirely possible that that could happen, and it may have happened. But I would have to take a look at the records in order to say for certain. However, let us assume it has happened.

Q. Let us assume it has happened. Therefore it will be possible that for one particular year a new policyholder will have received, by way of unabsorbed premium, more than he should normally have received from the underwriting profits? A. Well, if he had gone in at the beginning of the year and gone on to the end of the year, and he had received the dividend and the underwriting results showed a loss, he would have had an economic gain. Yes, he would; providing he was in the classification of risk where the

losses were suffered. If he was in a classification of risk according to hazard not responsible for the losses, he would not.

Q. He would not have received anything? A. He would not have received anything but what was his due.

Q. Would he not have received something from the investment income? A. He would have received his dividend.

I am perhaps inept in answering your question. My point is that if he was in the class of risk which produced the losses, he would have been paid a dividend because for all the operations of the company dividends are paid to all policyholders, and that is where the insurance company comes in, because it is the payment to the few out of the contributions of the many.

Q. Would you call that proportion that he receives, and to which he has not contributed, a gain from the business that he has transacted with the company? A. It may or may not be gain, as I said, depending upon the hazard classification in which his risk fell. His classification may have produced all the losses, and in that respect, for that year, there would be some economic advantage to him.

Q. Advantage to him which he did not gain himself, or which his policy did not gain? A. To which he has contributed but little. I am willing to admit that.

Q. In other words he has received contributions from other policyholders of previous years? A. Well, he has received his share of the distribution of the common fund.

Q. But in that common fund there is a certain amount of investment income? A. Oh, yes.

Q. That investment income is derived from the reserves which have been taken from the contributions of policyholders of former years? A. Yes. It cannot be done in any other way.

The first thing I noticed when I stepped out of the car was the cold. It was a sharp, biting cold that seemed to penetrate my very bones. I shivered as I walked towards the entrance of the building, my hands tucked into my pockets. The air was thick with a heavy mist, and the ground was slick with rain. I had never before experienced such a cold, and it made me feel like I was walking through a wall of ice.

As I entered the building, the cold didn't go away. In fact, it seemed to get even colder. The air was stale and heavy, and the walls were damp. I looked around, trying to get my bearings, but everything seemed so familiar and yet so strange at the same time. The corridors were long and empty, with a few flickering lights that cast a dim glow. I felt a sense of unease, a feeling that I was not alone, even though I knew I was.

I continued to walk, my footsteps echoing in the silence. The walls were covered in a thick layer of dust, and the floor was uneven. I noticed a small, dark spot on the wall, a shadow that seemed to be watching me. I turned my head, but nothing was there. I shook my head, trying to clear my mind, but the feeling persisted. It was a strange, almost hypnotic feeling that made me feel like I was part of something much larger than myself.

I reached a set of stairs and hesitated for a moment. The stairs were dark and seemed to lead down into a void. I took a deep breath and descended, my heart pounding in my chest. The air was even colder here, and the walls were even darker. I felt a sense of dread, a feeling that I was about to discover something terrible. I walked down the stairs, my hands outstretched, feeling for a handrail that wasn't there.

At the bottom of the stairs, I found a small, dimly lit room. The room was empty, except for a single chair and a small table. I sat down in the chair, my head buried in my hands. I felt a sense of despair, a feeling that I had been tricked. I had come to this place, and now I was alone. I looked at the clock on the wall, but it wasn't working. The hands were frozen in place, and the time was meaningless.

I stayed in the room for what felt like hours. The cold was unbearable, and the silence was deafening. I tried to think, but my mind was a blank. I felt a sense of hopelessness, a feeling that I was trapped. I looked at the door, but it was locked. I tried to open it, but the handle was frozen. I felt a sense of panic, a feeling that I was going to die here.

Just as I was about to give up, I heard a sound. It was a soft, rhythmic sound, like the ticking of a clock. I looked up, and the clock on the wall was moving. The hands were ticking, and the time was passing. I felt a sense of relief, a feeling that I was not alone. I stood up and walked towards the door, my heart pounding. I opened the door, and a bright light shined on me. I stepped out, and the cold was gone. I was back in the car, and I was safe.

I looked back at the building, and I saw a small, dark figure standing in the doorway. I felt a sense of fear, a feeling that I had been watched. I got into the car and drove away, but the feeling persisted. It was a strange, almost hypnotic feeling that made me feel like I was part of something much larger than myself. I had been to a place that was not real, and I had seen things that I should not have. I felt a sense of wonder, a feeling that I had discovered a secret. I was a part of something much larger than myself, and I was not alone.

Q. This investment income which is being paid in one particular year to the new policyholder does not actually represent gain to the old policyholders, does it? A. No. It does not represent loss to the old policyholders, either.

Q. It does not represent a gain earned by the new policyholder? A. Maybe not wholly.

Q. Then may I suggest that at some time it has represented a gain for the company as such? A. Oh, if you take the company strictly apart from those in whose common cause it operates, in that sense, that mythical individual created by law, yes. If that is your point of view that is right.

Q. I am not here to express any point of view; I am asking you your point of view. A. Yes.

Q. There are only a few other questions I should like to put to you. Could you tell us on which of the two alternatives set out in the 1942 income tax act in the United States your companies, or some of them, were paying last year and the year before? A. You mean the federal tax in the United States?

Q. Yes. I would refer you to page 8 of your brief, paragraph 38. On which of those two bases did your companies pay? A. Without looking at the record I could not say.

Q. But would it be possible -- A. I can furnish that information.

Q. -- that some companies paid under one, and other paid under the other? A. That is possible.

MR. HAYDEN: That is a fact.

BY MR. BROSSARD:

Q. In addition to this tax, are the companies called upon to pay state taxes in certain cases? A. Premium taxes? Yes.

Q. And is the rate of those taxes common to all states,

or does it vary? A. No the rate will vary from state to state. Presumably on the average it would be two per cent.

Q. Are there states in which the rate is higher than two per cent? A. For certain kinds. I think the state of Oklahoma has taxes paid under protest by about a thousand companies, or four or five hundred companies, stock and mutual, on an increase in taxes to four per cent.

Q. Those taxes are taken into account when you are computing the expenses of the year, I suppose? A. Yes, certainly in a mutual company, and I believe in a stock company too.

Q. And in so far as Canadian policyholders are concerned, they have to bear their share of those taxes? A. The policy holders in the pool bear their share of the tax load.

Q. So as it is at present, Canadian policyholders have to bear their share of these state taxes, and also their share of the federal tax? A. Yes.

Q. But you claim that as against that, the American policyholders have to pay their share of the Canadian premium tax? A. Yes, two per cent or three per cent. To me it seems almost even-Steven.

BY MR. ARNASON:

Q. Do all these states levy premium taxes? A. Yes. I think they all did but Connecticut, which taxed companies on a reciprocal basis, but they had a change in the tax law recently. There is this off-set to be carried again. Take the state of Illinois for example. It does not tax any domestic company for the Illinois premium tax, whether it is a stock company or a mutual company. I suppose that is a philosophy which is followed to some extent here in the dominion, of aid to local concerns;

to some extent here in the dominion, of aid to local concerns; and which is followed by the nation in our tariff law policy, and so on. But there is one heck of an argument in the United States now over this question of tax equalization of domestic and foreign companies.

BY MR. BROSSARD:

Q. Mr. Gruhn, when comparing the two per cent balance, let us call it that, or the unpaid unabsorbed premium which the company has retained over a period of years, with the relation of the amount of dividends paid by stock companies in regard to capital investment on the one hand, and with the amount of dividends paid in relation to the equity in the companies on the other hand, did you think of also comparing with this two per cent balance of the mutual companies the percentage of the undivided profits and dividends paid by stock companies in relation to the net premiums received by these companies over the same period of years? A. You have given me a rather long question. Whatever the compilation is, I am certain I did not make it. I have not prepared it, or I have not had it prepared. I call your attention to the fact that the two per cent you were talking about since noon has been reduced to something under one per cent.

Q. I know that it has. A. I have not such a compilation as you suggest; and of course I do not admit that this phraseology of "undivided profits" in connection with the two per cent has merit.

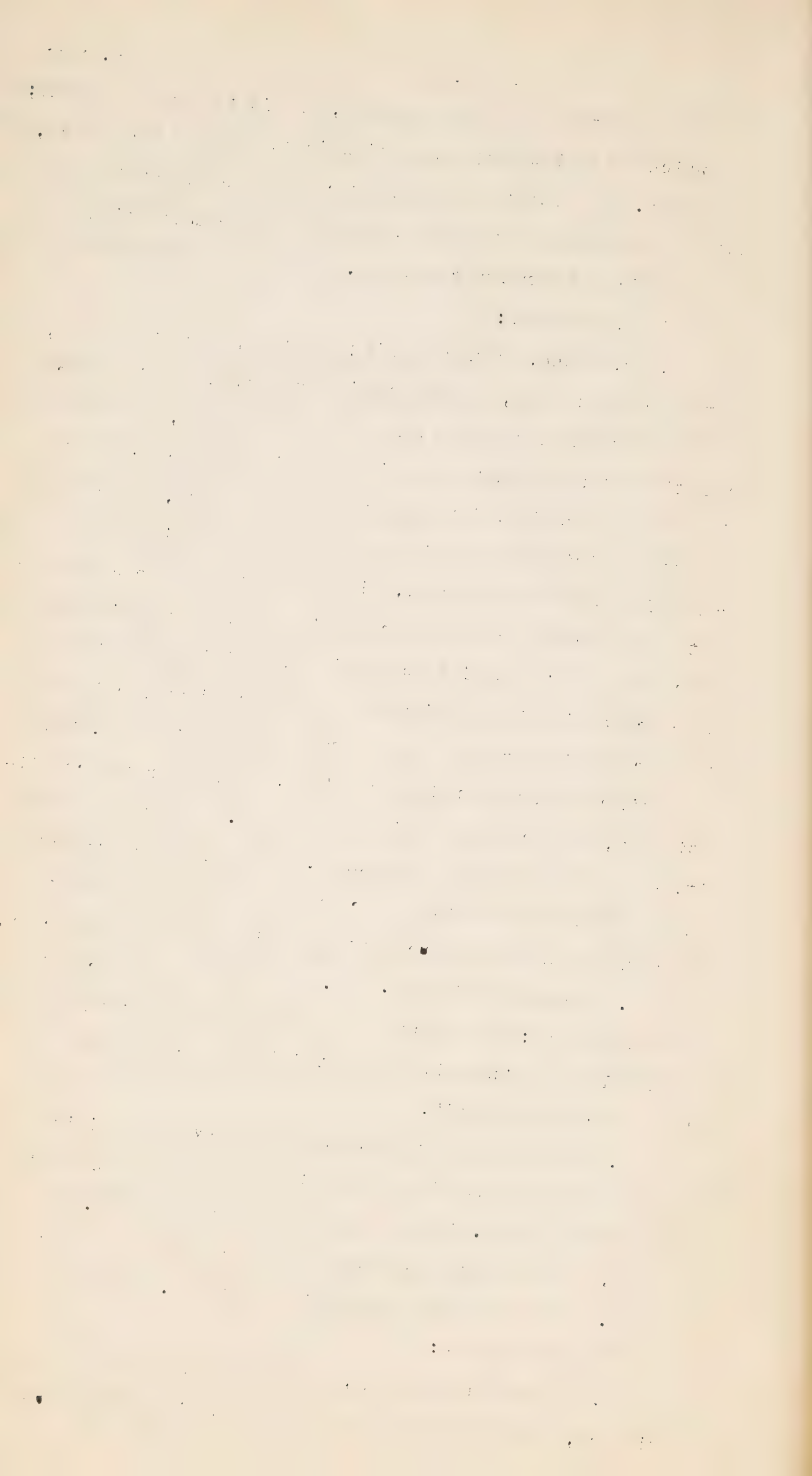
Q. Then let us say accumulated reserves and dividends paid in relation to the total net premiums paid during the same premium? A. I have not made the compilation.

Q. You have no idea what that percentage would be?

A. No, I have not worked it out at all.

BY THE CHAIRMAN:

Q. Is it proper to say, as flowing from the whole of your evidence, that the debate here before us is confined to



investment income revenue as to which, in the United States, until 1942 there was no tax, and that a tax was then put on by reason of war needs. Is that a correct statement, flowing from your evidence? A. I think the contention of the opposition goes much further than that.

Q. But does that statement flow from your evidence?

A. Will you please repeat that ?

Q. That the debate is really confined to investment income which was not taxed in the United States until 1942-- I am speaking of mutuals now -- and then was taxed only as a war measure? A. That is right.

Q. Mr. Freeman made a statement of that kind yesterday, also. A. Yes. I beg your pardon, Mr. Chairman. I apologize if I have appeared to debate. It was not my intention to do so. I may be over-enthusiastic , and I apologize. I think I am representing a good cause.

BY MR. BROSSARD:

Q. Mr. Gruhn, this will be my last question. Coming back to this question of state taxes in the United States, is that tax imposed upon the gross premium or is it imposed upon the premiums less dividends? A. In the main, on the net. In connection with life insurance companies, we have Canadian companies doing business in the United States. We have no Canadian mutual fire companies doing business in the United States; and I invite any of those present to come over the border, and we will treat them well. In connection with the life companies, the same situation is true.

MR. BROSSARD: That is all, my lord, as far as I am concerned.

BY MR. HAM:

Q. If I may venture to ask a question, Mr. Gruhn,

some time ago you advanced the pronostication that the joint stock companies would disagree with the figures you submitted with respect to, as I call it, the earnings on capital of American companies; of course, without the exhibit I cannot either agree or disagree with you. But I would like to be clear in my mind that these figures apply only to capital invested in those corporations? A. That is correct, provided that the capital takes also into account the shareholders' actual payment to surplus.

Q. The actual paid-in capital? A. Yes.

Q. And that it was only American companies in the list, was it? A. Oh, yes. I think I am justified in directing my attention to my American friends.

Q. I just wanted to be sure about that. A. The same situation might apply to some of the other companies.

Q. And it would apply to their world-wide business, I take it? A. Oh, no.

Q. It does not apply to Canadian business alone, those earnings? A. I do not know what proportion of those earnings come from Canada. All I have read is Mr. Baldwin's articles in the New York Journal of Commerce each year. Somehow I have gained the impression that the fire companies, particularly, in Canada, have done very well, because he kept urging rate reductions. I am like Will Rogers in that respect.

Q. The figures you supply in that statement would not prove that point particularly, would they? A. No. It proves over all in their operations that the companies are doing all right.

Q. In their general operations, as American companies? A. I am not admitting that does not apply to Canada. I reserve the right to take a look at that.

Q. I do not ask you to go that far. You mentioned this morning the difficulty with terms; and perhaps if I use the term "surplus" to refer to income after its outgo has gone, but leaving out "profit", we will not misunderstand each other. A. If you call it profit it is all right; I think you are very clear.

Q. I do not suppose you have information on this point, but I should like to have it if you have. Of the thirteen companies whom you represent here, do you know if any of them are members of one or the other of two what are called conferences, the Independent Fire Insurance Conference, or the Independent Automobile conference? Have you any knowledge of that? Perhaps you have not? A. No, I do not keep abreast of all their affiliations.

Q. Now with respect to the ownership of the company, every policyholder would have a right to vote; is that a fact? A. Yes.

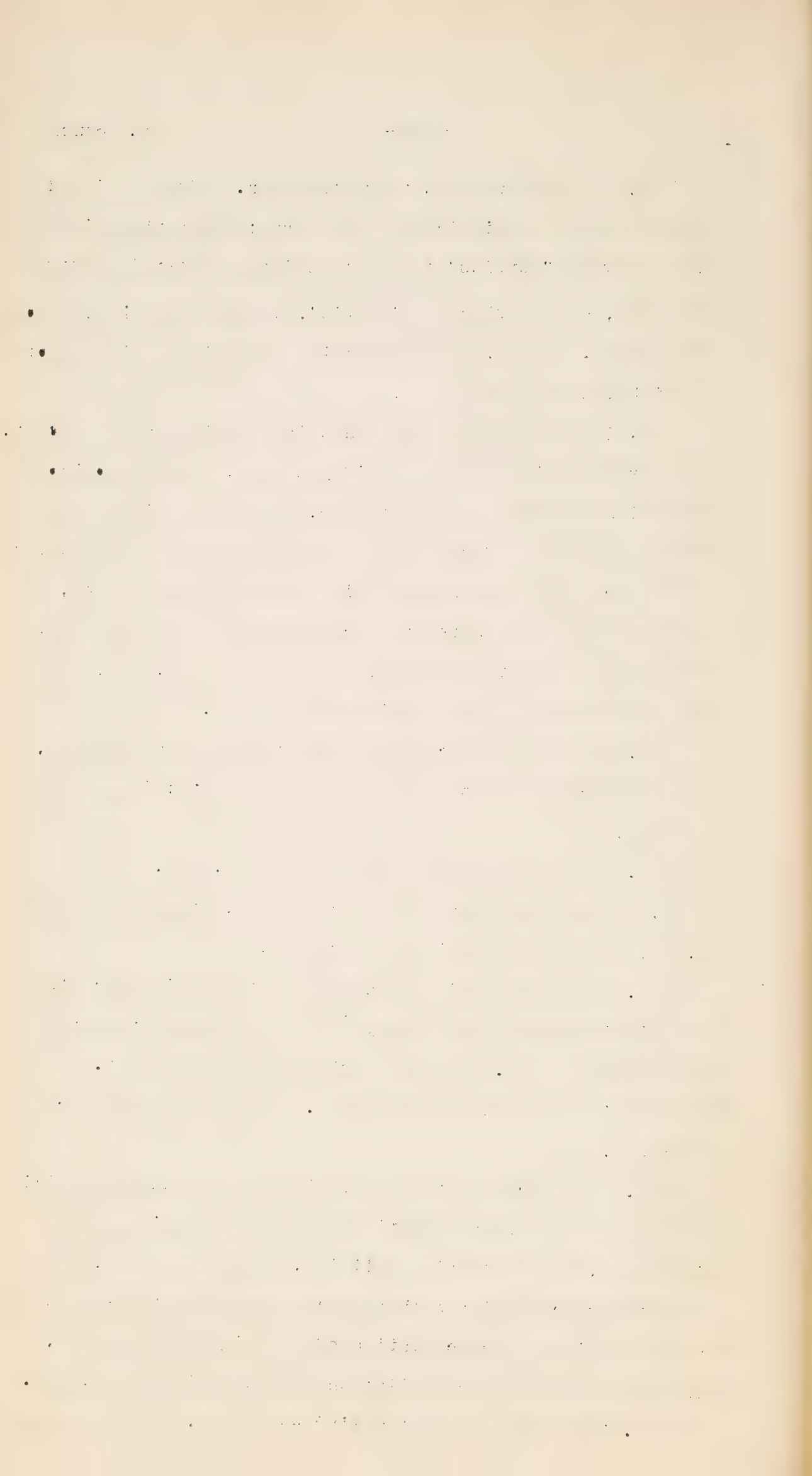
Q. If he attended the meeting? A. Yes.

Q. Is there any provision for proxies, or must he attend? A. No, there is provision for proxies.

Q. Is the provision with respect to proxies such that some individual has the proxy if the policyholder member does not attend? A. The member give it or he may not. He may give it to whom he pleases. The normal practice is followed.

Q. And of course those policies being standard policies, with the right of cancellation in them -- in fire policies in Canada, and automobile policies, and some others, there is a statutory condition with respect to cancellation-- you have the right of cancellation of the right of a member, as a member, by the cancellation of his policy? A. Yes.

Q. On the occasion of making -- A. That is not used,



however, for the purposes implied by the question.

Q. I do not suggest that it is. It is there, and it could be used, but I do not suggest that it is used for that purpose. Any underwriting gain would appear in your surplus, as I suggested; and to whose benefit or profit would that inure, when you have an underwriting gain?

MR. HAYDEN: If my learned friend is asking as a fact, that is all right. If he is asking for the construction of some words which sound very much like the provision of a certain income tax statute, surely the witness is not going to interpret an income tax statute.

THE CHAIRMAN: I do not think the witness needs protection.

MR. HAYDEN: I am not suggesting he does, but I am not going to get him into the capacity of a United States citizen interpreting Canadian law.

THE CHAIRMAN: I am quite sure he will say so if he does not want to answer.

MR. HAYDEN: I do not want him to be asked to interpret a Canadian statute.

BY MR. HAM:

Q. If I may repeat my question, any underwriting gain would appear in your surplus; and to whose benefit or profit would that inure, when you have an underwriting gain?

A. The whole tenor of my remarks and my discussion is to the effect that there is no underwriting profit that represents the kind of economic gain which is either income or profit under any tax law.

Q. I do not think I used the words, "underwriting profit." I think I said, "underwriting gain." You have an underwriting gain, in fact? A. There is the difference, naturally, when the policyholder pays in the premium and all of it is

used; all the premium is gone but if all is not used, part of the premium is left. As that expression is understood in trade, that might be regarded by some as gain, but in the mutual set-up it is not gain or profit.

Q. With respect to that difference which is left, to whose benefit or profit would it inure? A. It cannot inure to the profit of anybody. It is paid back as a refund, when it is paid back to the policyholders of the company.

Q. It goes to the policyholders? A. Yes, certainly.

Q. Do any of the members of your American Mutual Alliance writing business in Canada, write assessable policies, or are they all on the cash premium plan? A. Now you are using an antiquated term which has one meaning in Canada under the statute that is foreign to the proper application of it to certain mutual companies.

Q. I am sorry if I did that. A. Answering your question directly, as to the assessment liability, there is no liability for additional assessments.

Q. With respect to any of the companies members of your Alliance writing in Canada? A. I would say that is true of all of them, now.

Q. It is substantially correct, anyway. And the members of the Alliance write generally fire, automobile and casualty lines; that is correct? A. Yes.

Q. And with respect to this local fire business, would a substantial portion of their business be what is commonly known as farm business? A. No.

Q. It would be general insurance? A. Yes; unless you have a special definition of what farm business is in Canada.

Q. Oh, no. I think you as an American and I, as a Canadian, are talking about farm business and we mean the

same thing. Returning for a second to the question of a cancellation being subject to the various statutory conditions concerning fire insurance, automobile insurance, and other conditions in casualty policies, in those statutory conditions there is a short date penalty with respect to cancellation when the insured cancels? He does not get pro rata; that is a fact? A. That is, a policyholder, if he cancels, then the normal provision in the policy --

Q. A penalty is exacted? A. Well, I have not regarded it as a penalty. It is a differential in charge that represents a cost, I presume, which would apply in the case of stock companies as well as in the case of mutual companies, so therefore it is not a penalty, if it is a proper differentiation.

Q. He gets a smaller return premium if he cancels, either with a stock company or a mutual? A. Yes. That is a general provision in standard fire policies; and, as I said, mutual companies use standard policies.

Q. Well, such penalty or difference would appear in your surplus, if you had a surplus? It would go into the income of the company? A. It is an amount that is used. It is an expense, undoubtedly.

Q. But it increases the income of the company by the amount of the penalty, or whatever it is? A. It is a proper insurance cost, figured out and considered to be proper, and it is used by all companies, stock, mutual, reciprocal, whatever they may be.

Q. That is true; but would you suggest that anybody figured that out as being the exact cost of putting on a policy, or is it not more in the nature of a penalty, with no relation to cost? A. I do not concede that it is a penalty.

Q. Then when a policy is cancelled by an insured, he pays a higher rate per diem than he contracted to pay for his insurance? A. That is a proper part of the rating idea.

Q. It is a higher rate per diem for the insurance for the period? A. Call it what you will. If the company cancels, under the rating system it is a different rate than if the policyholder cancels.

Q. And which is the higher rate? A. The cancellation by the policyholder. You know that as well as I do.

Q. All I want is to get it on the record. The difference between the two rates of cancellation, then, would appear in your surplus, if you have a surplus? A. If it was not a charge that was used up it would appear in Finlayson's report as an underwriting profit.

Q. But assuming that it is not used up, it would appear in your surplus? A. If it was not used up in some other way during the year in the payment of losses. The minute something is not used, we do not pick it up and carry it off and dump it into this back pocket called surplus. It may be used up in losses before the year is up, or even before the day is up. I do not know.

Q. Having collected that amount, to whose benefit or profit does it inure? A. No benefit or profit. There is no use coming back to that proposition, because I have contended during the whole day that I have been standing here, and trying to convince you that I do not agree with your theory of what mutual insurance is.

Q. Ultimately it would get back to the pockets of the policyholders; is that correct? A. Anything in the company that belongs to the policyholders is theirs as a matter of right.

Q. You mentioned this morning, with respect to investment,

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that, like all insurance companies, the companies you represent have investments, and they have income from those investments and that income would appear in the surplus?

A. If it was not used up.

Q. And would ultimately get back to the pockets of the policyholders? A. We do not follow it through. We do not have a bird dog following through where the money goes. I have given complete testimony to the fact that under the accounting practices of our bureau of internal revenue, investment income is first considered as having been used to pay losses and expenses.

Q. And the balance, if any, inures to the benefit of the policyholders? A. There will not be any balances in our companies on that basis, because the investment income is not large enough.

Q. You do have a policy dividend? A. We make refunds of unabsorbed premiums to policyholders. That is what bothers our competitors.

Q. It does not bother me? A. Well, you are not a competitor. You are a hired man, like I am.

Q. I think that has some advantages, at that. A. I think there is more intelligence among some of the hired men than among the company executives, I am free to admit.

Q. I think I have only a couple of more questions. A. I am perfectly glad to answer them if I can.

Q. Your companies, among others and with others, accept reinsurance? A. I said that in the beginning.

Q. And on that reinsurance there is the payment of a premium or reinsurance commission? A. Oh, yes; reinsurance received to pay off reinsurance issued. It may balance out in a given year. You may get on the wrong side one year

and on the right side another year. Our objective in the main is to spread the loss. We have to be good underwriters.

Q. But on that reinsurance venture, for which you will receive a premium, you may make a profit or a loss with respect to reinsurance itself? A. There may be a difference in the particular year, but over a period of time it may wash out.

Q. But in any accounting period there may be a profit or a loss on those reinsurance transactions? A. Subject to the difference in our conception of what profit and loss is.

Q. Well, there may be a gain, then, if you take in more in reinsurance premiums than you pay out under reinsurance contracts. You may have something left in your pocket?

A. And not a taxable gain.

Q. I am not saying whether it is taxable or not. You have a gain? A. There would be a difference.

Q. More money in your pocket than you had before?

A. Not my pocket.

Q. In the pocket of your company, then; I am sorry. There would be a gain, a difference, a plus? A. Yes, there would be a difference. You understand what I mean?

Q. And that would go into your surplus? A. It might be used up in losses. I do not know where it would go. It depends upon the operations of the year.

Q. It would go in with your income, if your outgo did not exceed it? A. It would go into the bank until used.

Q. And as long as you controlled the bank account that would be your income, would it not? It would be in your income? A. Yes. I said all that.

Q. And being in your income it would inure to the benefit

or profit of your policyholders. Is that a fact? A. I do not say that it inures to the benefit or profit of the policyholders at all.

Q. To whom does it go, then? A. It may go in losses.

Q. It would be income to begin with? A. It is a receipt at a given time. You may pay it out.

Q. But if your disbursements are less than your receipts, you have a balance? A. Yes, sure. I have said that all day long.

Q. And that gain would affect the amount of that balance, would it not? A. The balance at a given time would be a little larger; yes.

Q. And it would ultimately get back to your policyholder, either by way of dividends -- A. I should hope so, if it were not used,

Q. That is the principle of your operation, that it would get there? A. We operate in the interests of the policyholders. I must admit you are right about that.

Q. One more question with respect to that. You said in your brief that you did not issue policies to non-members? A. That is right.

Q. How is that reconcilable with the issuance of reinsurance policies to other insurance companies?

A. Well, there is a question which has not been settled, as to whether that is a policy or another type of contract, which is necessary for the convenience and use of the company in transacting the insurance business.

Q. It is an insurance policy? A. Some call it a policy and others call it a contract. In a sense that is no different than contracting for supplies or for other needs of company operation.

Q. It is on a policy form in many cases, is it not?

A. It may be. It is a contract, as differentiated from a policy.

Q. It is likely on a policy form, for which the premium is taken; and that is called a premium? Is that correct?

A. No.

Q. It is never on a policy form? A. I would not say it was a policy form.

Q. Would it be in the same wording as a policy issued? Would the general skeleton of the form be similar?

A. I do not pass upon the reinsurance contracts of the companies. I would not know how they are worded.

Q. I take it, then, you do not know? A. All right; I do not know.

Q. Does a policyholder who has had a loss participate in a dividend? If he has had a loss on his policy, would he get his dividend, if one were declared? A. In the main, yes.

Q. Generally speaking? A. Yes.

Q. In appendix 5 of your first submission, you list certain dividend resolutions as examples of the type of resolution usually adopted; you refer to the Manufacturers Mutual and the Hardware dealers? A. Yes.

Q. And I note that in these resolutions the dividends are fixed at the time they are passed, and they are to remain until they are changed? A. That does not necessarily follow. Some boards make a dividend declaration once a month, some every three months, and that varies in different companies.

Q. The resolution of the National Retail Dealers, that is one type where they fix them until changed; and others are fixed for a stated period? A. I am not so sure that applies in the National Retailers; I really do not know.

Q. It is in the brief, and we can see it. I think

that is all I have, thank you, Mr. Gruhn.

THE CHAIRMAN: Is there anything further?

BY MR. ELLIOTT:

Q. This is really perhaps a matter of argument rather than a matter of fact, but it is a point on which I would like to have your opinion. You believe that income and excess profits taxes do not enter into the determination of the premium rates of joint stock companies? That is what I understood you to say? A. That is my opinion.

Q. And that if any tax is imposed upon a mutual company, it does affect the net cost of insurance to policyholders? A. That is right.

Q. I take it that your opponents might advance this argument: that the dividends you pay include, at least some part of it includes, a payment for the same sort of services that the stockholders of a stock company give; that is to say, payment for supplying the funds that enable the company to carry on. That question is perhaps too long?

A. May I restate it this way, and see if I am correct in my understanding. If there is a small sum left over, you mean--

Q. No, I am speaking of the part that is returned to the policyholders. Is it your contention that the amount of it is not affected by the amount of policyholder funds that the company receives? A. From investments, you mean?

Q. Well, it has to have these funds to carry on insurance, and you say investment is a necessary but incidental factor. Investment income is one thing?

A. You mean is it my contention that the investment income does not affect the amount that the policyholder contributes?

Q. No. The size of the investment income will affect the amount that the mutual can return to the policyholder?

A. Oh, yes; no matter from which pocket you take it, when you take the sum total of the funds, if you have some investment income it diminishes the fund that you collect; certainly.

Q. It either diminishes the expense and loss, or -- ?

A. It depends upon the policy the company pursues. Oh, yes.

Q. My understanding of the argument of the stock companies, or the position of the stock companies, is that they contend that the repayments, the returns, the savings, or whatever you call them, that you make to your policyholders, contain an element of investment income, shall we say?

A. Oh, yes. They go further than that.

Q. I know; but I am not going as far as they go. But they might take this position. The income and excess profits tax do, initially at least, tend to diminish the amount credited to shareholders' account in a joint stock company?

A. I think that would naturally follow.

Q. What would you say to the proposition that similarly a tax imposed on what the joint stock companies call your income would diminish the amount returnable to the people who furnish your investment fund?

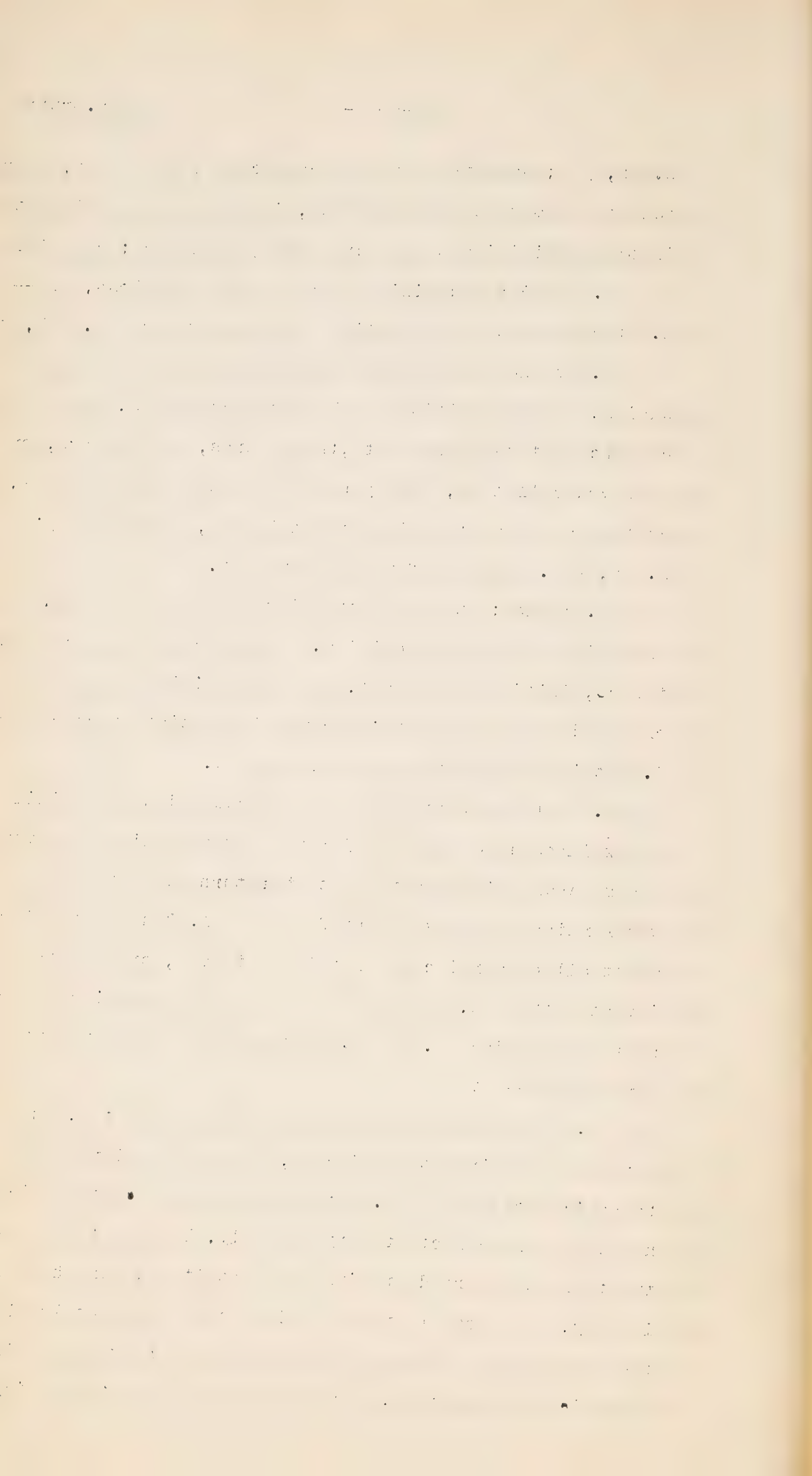
A. You are talking about all of our income that is left over, or just the investment?

A. I am talking about a tax applied on any part of your income.

A. A tax applied on any part of our income --- ?

Q. I am not speaking of a gross premium tax, but say a tax on your investment income, or on the returns you make to policy holders?

A. A tax on returns made to policy holders would affect it very severely, because that would treat the unabsorbed premium as a profit and take half of it away, and I say that is unfair because that would give the investor in a stock company an opportunity to obtain a particular advantage, because he is getting the policy-



holders' money; he is a third party who gets the benefit of it and should pay a tax on it. The policyholder, in part of his premium, contribution that he gets back, is getting a return of something he paid, and not profit; so that would affect it very severely. That is what we have been opposing in the United States and shall oppose here, to the best of our ability.

As to the investment income, or answering your question directly as to a tax on any part of our income, it would react unfavourably to the policy holders, certainly.

Q. And your position is that it would react unfavourably on your policyholders, as policyholders? A. That is right.

Q. Not as furnishers of the funds that allow the company to carry on? A. If you mean in the sense he is not furnishing funds, he is making a premium contribution that is no higher than he would make anywhere else. In that sense he is furnishing the funds in the mutual or stock company. I would say that to tax him as a shareholder would be particularly burdensome. You are already taxing him as you would tax him, as we tax him in the United States, because you have substantially now the same tax on him that we have in the United States.

MR. ELLIOTT: Thank you for your patience.

THE WITNESS: Thank you, sir; and, Mr. Chairman, I want to express my deep appreciation for the courtesy extended to a foreigner.

MR. HAYDEN: I should like to have leave to file this reinsurance agreement. I will procure a copy of it, if I may file it later on. It is the form which is used for this procedure of reinsurance.

MR. PARKER: Mr. Chairman, the situation is this. There is a brief of nine pages of material presented by the Farmers' Mutual Insurance Companies of Ontario. They have no counsel. They are representing a group of farmers who have been sitting for some time, and I am advised that they are very anxious to get away to-night if at all possible. I have gone through the brief pretty carefully. I doubt if it will require any examination at all; certainly not more than half a dozen questions; and if your patience would permit you to assist these gentlemen to get away to-night, I think we can read it in ten or fifteen minutes and have it disposed of.

THE CHAIRMAN: I think we are quite prepared to do that.

MR. PARKER: That would be appreciated by them very much.

THE FARMERS' MUTUAL INSURANCE
COMPANIES OF ONTARIO

MR. ROBERTSON: Mr. Chairman, this is Mr. Walter R. Cross, who is the secretary of the Ontario Mutual Fire Underwriters' Association. He is going to present his own brief, which he will read; and if any examination is requested he will be quite happy to subject himself to it. He is the manager of the oldest farm mutual in Ontario, which I believe was incorporated in 1856; and he is secretary of the association, which is an association of all the farm mutuals, sixty-eight in number, operating in Ontario under the Ontario Insurance Act.

MR. WALTER R. CROSS,

Secretary, Ontario Mutual
Fire Underwriters' Association,
having been duly sworn,
testified as follows:

THE WITNESS: Mr. Chairman and gentlemen of the Commission, first may I thank you, on behalf of our members, for your

consideration, which made our submission possible at this time rather than in Toronto as originally planned. I may say that since that time our association has held its annual meeting, and I now speak for all the members of this association and for the committee which they appointed to make this presentation to you in their behalf.

"We are pleased to provide as requested, ten copies of each of the following:

- Association By-laws
- General Company By-laws
- Company Contract Forms
- Additional Data.

We believe these will give you a complete picture of our methods in serving some 140,000 rural policy holders throughout the province of Ontario.

"Our association does not feel that our member companies are co-operatives under the terms of the directive to the Commission under P.C. 8725, but as farm mutual fire insurance companies in other provinces have been referred to in other briefs presented for your consideration, we feel that a presentation of our principles and functions would be of interest to the Commission.

"Our association consists of all farmers' mutual fire insurance companies in Ontario (65 in number) whose business is over 90 per cent rural, and 2 farmers' weather companies of like nature. Our operations are confined to Ontario only. The average company serves about 2000 members, and carries about nine and one-half millions at risk."

If there is any further information you would like in connection with the association I will have filed with you, if you care to have it, a copy of the last annual convention,

in which is incorporated the auditor's report as to the very modest budget under which we operate. We budgeted last year a total amount of \$1,300 in carrying on the work of the association.

"The companies have no subscribed capital, and are entirely mutual in character. They are officered and directed by their own farmer members exclusively. They were organized by farmers, and have but one purpose, namely, to provide their farm members with sound insurance at cost.

"The members of these unique organizations all help to produce the only service being sold, namely, protection from disaster. Since no business is done with non-members, and no capital is subscribed, each contributes directly and equally in producing and purchasing the company's only stock in trade -- protection. This type of mutual effort has provided insurance in the unprotected rural areas of our province for nearly ninety years. Had it not been for this outstanding development in rural endeavour, the farmers of this province would be paying much higher rates for their fire insurance. We submit then, that these institutions should be encouraged by government to continue their efforts on behalf of the farmers, whose lot has never been an easy one. Over 80 per cent of the farm buildings are insured by the local mutual company, and in certain districts, 95 per cent of the business is in the local company. This is evidence of the extent of their worth to the farmer, and the satisfactory discharge of their function.

"The companies which this association represents operate under the Insurance Act, chapter 256, R.S.O. 1937.

"The relevant sections are Section 1, paragraph 43 and Sections 112 to 127 inclusive of the Act.

"The following provisions of the Act (from amongst those

The first part of the book is devoted to a general
introduction of the subject. The author discusses the
importance of the study and the scope of the work.
The second part of the book is devoted to a detailed
description of the various methods used in the study.
The author discusses the advantages and disadvantages of
each method and the results obtained from their use.
The third part of the book is devoted to a discussion
of the various factors which influence the results of the
study. The author discusses the effect of the different
factors and the ways in which they can be controlled.
The fourth part of the book is devoted to a discussion
of the various applications of the study. The author
discusses the ways in which the results of the study
can be used in practice and the benefits which can be
derived from their use.

above mentioned) are as follows:

"Section 1, paragraph 43:

"Mutual insurance" means a contract of insurance in which the consideration is not fixed or certain at the time the contract is made and is to be determined at the termination of the contract or at fixed periods during the term of the contract according to the experience of the insurer in respect of all similar contracts whether or not the maximum amount of such consideration is predetermined.'

"Section 112, subsection 1:

'The insurer may accept the premium note of the insured for insurance and may undertake contracts in consideration thereof and such notes shall be subject to cash payments and assessments for the losses, expenses and reserve of the insurer in the manner hereinafter provided.'

"Section 114, subsection 2:

'The cash payment required at the time of the application for insurance of agricultural property, other than brick, stone or concrete dwellings, may be reduced with the approval of the superintendent by the directors when and so long as the surplus of the insurer is not less than twenty-five cents for every one hundred dollars of the total net amount at risk. R.S.O. 1927, c. 222, s. 106 (2); 1937, c. 72, s. 29 (3).'

"Section 114, subsection 4:

'"Surplus" as used in this section shall mean the assets of the insurer other than the premium note residue after deducting therefrom all liabilities of the insurer (other than contingent liabilities or unmatured contracts) and the proportion of cash payments and instalments thereof paid in advance applicable to unexpired policy contracts calculated as required by subsection 5 of section 73. R.S.O. 1927, c. 222,

s. 106 (4); 1932, c. 24, s. 5; 1937, c. 72, s. 29 (4).'

"Section 114, subsection 5:

'States that before a refund from surplus may be made by a company, its surplus in cents per one hundred dollars of net insurance in force must be equal to the following schedule, and then only after approval has been obtained from the Superintendent of Insurance for Ontario.'

SCHEDULE

"When the net amount at risk is greater than
\$25,000,000 - \$0.60

"When the net amount at risk is greater than
10,000,000 - .70

"When the net amount at risk is greater than
5,000,000 - .80

"When the net amount at risk is greater than
2,000,000 - 1.00

"It will be observed that the premium notes are subject to payments and assessments, losses, expenses and reserves and it will be further noted that the legislature while contemplating a greater proportion of the income might be used as surplus or reserve, provided that at least 25 cents for every \$100 of amount at risk must be held for reserves and for protection against future losses."

Those of you who listened to the Quebec brief this morning will observe that we are on a much sounder foundation in Ontario. Of course we should be, having been in business for some one hundred years.

"These provisions make it abundantly clear that the surplus of farmers' mutuals are not accumulations of income, but simply premium stabilization funds. These surpluses are accumulated from premiums collected at slightly higher than current necessary levels so that in good times when the loss ratio is low, moneys may be accumulated in reserve to meet losses at other times and to level off the premium and prevent drastic

advances when the loss ratio rises."

It is common knowledge, I think, in the fire insurance business that in bad times we have high losses and in good times we have low losses.

"In considering the income of a farmers' mutual fire insurance company it might be well to think of the original methods of collecting this income. When our companies were first organized, losses were paid during the year from borrowed funds, and at the end of the year an assessment was levied on the premium notes held by the company for an amount sufficient to meet the losses and the modest operating costs. This system was in vogue until 1924, when it was considered the part of wisdom to strike as nearly as possible an even annual assessment on the premium notes in an endeavour to place the business on a more stable basis."

That, I think, will answer a multitude of questions with regard to the rate structure.

"In spite of this wise precaution, many companies found it necessary during the depression years to levy special assessments against their members in order to meet their losses."

Speaking, as I do, as manager of the oldest of the farm mutuals, I say that during the years 1930, 1931 and 1932 we found it necessary to levy three extra assessments on the notes in order to meet our losses, which at that time were catastrophic.

"We should like to make clear that present surpluses have been accumulating for two specific reasons:

"(1) During the past five years, the farming industry has enjoyed a measure of prosperity and the surplus has been built up to weather the eventual readjustment period."

I am sure we have all heard a great deal about that great readjustment period.

"(2) It was considered more patriotic to leave the surplus in the company's hands for the purpose of buying blocks of Victory bonds to assist in the war effort, rather than lower the rates or make small refunds which would not be directed to the assistance of the war effort."

There are motions of some of the companies verifying that statement.

"As evidence of the sterling character of our companies, and their truly mutual outlook, two contributions made voluntarily might be mentioned.

"(1) The British Aid Fund of 1942-43, in the amount of \$86,169 was raised and sent for the relief of bomb victims in rural England.

"(2) A fund of \$48,390 was raised during 1923 to assist in the relief of farmers in Northern Ontario, whose properties were destroyed in the terrible conflagration of that time."

This was evidence of the purely mutual character of the companies. Our companies were under no direct obligation to make that donation.

"Our companies act as fire prevention units. We endeavour through inspection, education, and advertising, to acquaint our policy holders with all fire hazards, in an effort to have them removed. (See Appendix "A"). During the last three years over \$40,000 was spent on fire prevention work, exclusive of inspections, by our companies. Surely this is a commendable effort in rural communities which have long been denied the security of modern fire protection. Indeed, in a number of cases, rural fire fighting apparatus has been provided wholly or in part by our companies. In other cases, rural fire brigades have been organized. This is not a selfish effort,

since all enjoy the accruing security and freedom from fear. As a result, fewer fires occur, with correspondingly lower rates to members. It is well known that when a barn burns, the farm often reverts to pasture, with a subsequent reduction in assessment and loss of revenue to the township, as well as the general detriment of the rural community. These services to the farming community have never been, and are not now, rendered by other companies, although when they do accept farm risks, the rates are usually much higher than the cost of insurance of the same risks with farmers' mutuals.

"We as an association have been greatly interested in food production during the war years. At our annual meeting in March of 1942, the companies accepted a challenge to endeavour during 1942, to reduce losses --"

The idea was to thereby save the precious food which was needed.

"-- by 25 per cent of the previous five-year average. A determined effort was made, but losses were only reduced \$74,000 or 7.9 per cent. In 1943 a reduction of \$15,000 or 1.6 per cent was achieved, and during 1944 losses jumped by \$176,000 or 18.8 per cent over the five-year average; (see appendix "B") this in spite of a vigorous and increasing fire prevention effort."

I will go into detail on that if you wish, but I do not think it is necessary at the moment.

"Figures such as these in Appendix "B", representing recent loss experience, vindicate the necessity of establishing reasonable premium stabilization funds.

"Let us now refer to facts brought in two five-year periods, (see Appendix "C") viz. 1930-35, and 1940-45, with respect to the experience of our companies. In 1930 our companies carried \$639,210,000 of insurance, with losses of

\$1,808,000, when their combined surplus was only \$688,000, or 10.8 cents for each \$100 of insurance in force. I think, Mr. Chairman, you will agree that the directors of our companies at that time were stout-hearted indeed, and that they carried a great burden. These figures make clear that the farmers' mutuals carry on for protection alone, and without any profit motive to which income or profit taxes could reasonably apply.

"In the year 1931 alone, premiums were added to by way of special assessment on the premium notes by \$515,000, and still the surplus position of the companies was further depleted to \$316,000, or a mere 5 cents per \$100 of insurance in force. During this time, and for the next few years when assessments were necessary to meet losses, many directors would have been very thankful to have been relieved of their responsibilities.

"This however was not the course they chose. Instead they fought on, strengthened by the faith and loyalty manifested by their members who had accepted the assessments and the reduction of inflated policies. They removed hazards from their premises, and unfaithful members from their ranks, and gradually the improvement came, assisted by somewhat more prosperous trends in farming, until now, at the end of 1944, the average farmers' mutual in Ontario has 81 cents of surplus for each \$100 of insurance in force, with only one special assessment made during the last five years. This is indeed an outstanding achievement, but the sinister hand of rising loss cost hangs heavily over our heads. Losses have increased by \$250,000 from 1942-44, and present indications are that during the next few readjustment years we will again suffer losses, probably greater than in 1931, when they were \$1,200,000 more than in 1944."

I quote those figures to point out to the Commission the necessity of having a surplus of premium stabilization funds or accumulation of funds, or whatever you call it, for the protection of our policy holders.

"From these figures it will be seen that premium stabilization funds are necessary, and help to build up in good times to take care of the bad. In good times losses are low and money plentiful, but in bad times losses are high and money is scarce. This works out much the same as unemployment insurance. Another deduction which is quite evident is the uniformity in the amount of insurance at risk over the ten-year period, which has remained practically static --"

That, too, will answer the questions with respect to the participation of a member in a mutual company at this time, who may not have been a member at another time. Our membership is practically static, as is borne out by the figures in these tables.

"--except for reasonable variations caused by the fluctuation of values. The farmers' mutuals confine themselves to rural fire insurance, and offer no competition to other companies which do not want this type of insurance, and cannot therefore consider farmers' mutuals as competition.

"May we point out the original purpose for which these companies were organized -- to provide their own members with insurance at cost. May we also point out that the conditions of their licensing by the provincial government (under R.S.O. 1937, Chapter 256, of the Insurance Act, and part 16 of the Companies Act, Chapter 251) controls the following:

- (1) The type of risk they may accept.
- (2) The minimum rate to be charged.
- (3) The limits carried without reinsurance.

- (4) The amount of surplus necessary before rates may be reduced.
- (5) Supervision and approval of all contract forms.
- (6) Investment of surplus funds.

"Subject to the above, our companies still operate on the same basis on which they were organized, and they still have but one purpose, the sharing of losses by members of our farming communities. These districts were never served by any other insurer in the same way. Indeed, it was out of dire necessity that the original members banded themselves together for their mutual protection."

I have a copy of the original organization meeting here, in 1856. I will read a paragraph or two from it, if you wish?

THE CHAIRMAN: I hardly think that is necessary.

THE WITNESS: Very well, sir.

"It is worthy of note that these companies have served so well, that no new company has been organized during the last thirty-five years, to enter this field. It should also be stated that no farmers' mutual has extended into other branches or fields which others might have been serving.

"From the above it will be observed that farmers' mutuals are truly non-profit organizations and that their surpluses so-called are merely advance premiums held against the contingency of future losses and for the purpose of levelling out the premium cost so that such cost will not require much variation from year to year, although losses may vary greatly from year to year.

CONCLUSION

"We submit that it is NOT IN THE PUBLIC INTEREST to impose income or profit taxes on farmers' mutuals for the following reasons:

"(a) They are non-profit organizations and none of their income as received from year to year, whether paid out in losses, returned to members or passed to reserve to protect against future losses can be considered as taxable profit or income.

"(b) They are now and always have been true mutuals, insuring none but their own members and furnishing protection at cost.

"(c) The membership is almost completely static and the members of ten years ago who then contributed premium moneys remain members to-day, so that it can reasonably be said that any moneys distributed to-day, whether derived from last year's premiums or premiums paid ten years ago, are distributed back to those persons who originally paid the money in.

"(d) The farmers' mutuals do not constitute competition to the other companies who complain of unfair competition because the other companies will only write selected risks, and do not wish to accept farm risks generally. The farmers' mutuals operate in a field unattractive to the stock companies, and where they have not and will not furnish protection.

"(e) In the absence of farmers' mutuals the farmers, a section of the community which has always been in receipt of the lowest per capita income, would be required to pay very high rates for fire insurance protection. It is therefore not in the public interest that farmers' mutuals should be taxed, either by way of premium tax or under any kind of income or excess profits taxation.

"(f) The farmers' mutuals have effectively provided fire protection and prevention for the largest industry in Canada, at the lowest possible rates, and in the public

interest should be encouraged and supported, and should not be made subject to income and excess profits tax at the request of stock companies which have avoided assuming farm risks and are in business to make profit in all ways possible, including the selection of choice risks.

"(g) The cost of insurance by farmers' mutuals at low rates does not result in the farming community unfairly escaping taxation, because the cost of insurance being low, the deductible expense of fire insurance is less, and the saving consequently shows itself in larger profits which are at the present time subject to taxation under the Income Tax Act.

"All of which is respectfully submitted on behalf of the Farmers' Mutual Insurance Companies of Ontario, by The Mutual Fire Underwriters Association of Ontario."

Mr. PARKER: I have just one question to ask this witness.

Q. Perhaps, Mr. Cross, you will turn to the table attached to your brief. It shows that in 1944 there was a total surplus on hand for all these companies of about \$5,500,000? A. That is right, sir.

Q. And the total number of members, I think you said, is approximately 140,000, is it? A. Approximately 140,000.

Q. If you divide that total amount of surplus among the total number of members it would work out at around \$30 or \$35 each? A. I think that computation would be correct; about that.

Q. And I suppose the greater portion of that \$5,000,000 is invested at the present time? A. I would say so; yes.

Q. In Victory Bonds and other good securities? A. Largely in Victory Bonds.

Q. A pretty liquid type of security? A. Yes; necessarily so.

Q. That \$5,000,000, or the portion of it which is invested yields a pretty big income in the aggregate, does it not?

A. I would say it would yield possibly at two and a half per cent, and I would say that possibly \$4,000,000 of it may be invested.

Q. Nothing less than three per cent income at the present time, I would not think? A. There would be considerable of those funds which would be in trust accounts at two per cent.

Q. The amount is of no significance; it is a question of principle. Do you say that investment income is not income in the name of these respective companies? Why, if it were large enough to bear tax, should it not pay income tax? A. It has grown from \$316,000 at the low period in 1931, which was undoubtedly very low, as you say only 5 cents per \$100 of insurance carried; and you skipped the years from 1934 to 1940 -- ? A. I did so because they were just a sort of repetition.

Q. I am not suggesting anything else, but it does bring out very clearly that during the war years you have certainly very greatly improved your position. It has jumped from around 15 cents per \$100 up to 81 cents, and your total surpluses from around \$810,000 up to \$5,400,000. That is a pretty great improvement, is it not? A. It is a very great improvement; but if you will refer to my table on page 3 you will see that before a distribution of that surplus could be made the act requires that we have 60, 70 or 80 cents or even 100 cents per \$100 of insurance, varying with the size of the company, so we are just now getting to the point where we fully comply with the requirements.

Q. I am not suggesting for a moment that your surplus is too big. I am merely calling attention to the fact that during this war, which everybody has been struggling to help pay for,

this group of companies, whether its position was good or bad before the war, did improve that position to this extent, and in the process have not been paying income tax, that is any of these companies? A. That is true.

Q. Take a company with which perhaps you are more familiar than some of the others. Take the share of this surplus which belongs to each member. Is that allocated, or how does each member get his share, his \$30 or whatever it may be? How does it ever get back to him? A. It gets back to him in the low rate that he gets all during his time on his insurance; or it gets back to him in the form of a refund from surplus which is given to him in the reduction of premium one year, perhaps.

Q. Does he from time to time get actual cash refunds on his premiums? A. He does.

Q. That has been done from time to time? A. In isolated cases. It is just in the last five years that the act has been amended to allow for refunds from surplus.

Q. During that last five years have you been giving some refund of some portion of your surplus? A. I would think I might say that six or seven companies have done so.

Q. That is, those have been in a financial position where they thought it was safe to deplete their surplus to that extent? A. That is true.

Q. I would like your explanation, then, as to why or on what principle you say that the investment income of these companies is not income of the companies, with which the directors can do as they like, and why it should not be taxed as income? Will you just explain that? A. Well, Mr. Parker, that investment income is no different from premium income.

Q. Is it not? A. It all inures to the benefit of the policy holder.

Q. I grant you that, sooner or later. Is it allocated to him? Can any policy holder go to his company at any time and say, "You have some surplus there, and I am getting out and I want my share"? A. No, he does not do that.

Q. Supposing he gets out but leaves his \$30 behind. Who loses then? A. There is another consideration, sir, that he assumes when he goes into that mutual where he has a \$30 surplus. He has already signed possibly a \$300 obligation in the form of a premium note, which he must sign and assume before he can enjoy the lower rate procurable by the mutual system. If he is released from his note -- of course, mind you this does not happen; our policy holders go on. I have farmers on my lists who are third generation members of this company.

Q. I do not doubt it; but I will venture to suggest that you can also find some members who are in there for a year or two and then get out? A. Yes, sir, and who have come back since.

Q. Let us deal with them as they go out. Do they take this share of the surplus with them, no matter how small it may be? A. No, they do not do that, because it would not be practicable.

Q. Now, do not argue with me; I am not saying it would. Take one who went out and never came back. What ultimately becomes of his \$10 or \$15 or \$20, or whatever it was? A. Whether or not he had \$10, \$15 or \$20 depends entirely on the state of the company when he came in.

Q. He would have a little in any case, would he not? A. May I draw this to your attention, in the matter of refunds. Supposing we are declaring a refund to-day. The act says that unless a member has been a member for at least three years he does not participate in that refund. He must have been

there for some time in order to help build it up.

Q. Take the man who has been there for his three years, and has helped build it up. Then for some foolish reason or other he got out and said, "I want to take my little share with me." Is there any principle under which he is entitled to it? A. No.

Q. What becomes of it? A. It becomes the property of the remaining members who have assumed his liability while he was with them. Do you not think that is reasonable?

Q. I have no opinion one way or the other; I am merely trying to find out what happens. There is just one thing I want to call your attention to in these tables, that is the big sheet. Is that six cents per \$100 of insurance in the right hand column? A. Yes, that is per \$100.

BY MR. VAUGHAN:

Q. Do you know why the losses are so much higher in bad times than in good times? A. Yes, sir; I think I know. There are three reasons. One is that heating equipment becomes worn out, and roofs get in a bad state of repair. That is the first reason. Then there is the old business of shortage of help, because things have to be done in a hurry when there is not sufficient income to pay for the necessary help to take care of things, and it involves good housekeeping, whether it is in the barn or in the house. The third reason is the moral hazard, and that moral hazard is one of the things that we as farm mutuals have to contend with all the time.

Q. What does that mean, "moral hazard"? A. Do you want me to be specific? In the inflation following the last war many buildings were insured pretty well. Then came an influx of new Canadians, and some who had been here quite a while, to the mediocre farm lands, on which were situated buildings

pretty well insured. We are the only people who will pay cash for old buildings. There is only one stipulation; they have to be burned. There is the moral hazard.

Q. I do not question your explanations; I think they are reasonable enough, but it is rather odd when one reads the statement that in bad times losses are high and money is scarce. I just wondered about that. A. If you will take time when you are in Toronto to drop into the Department of Insurance they will show you graphs over periods of years which show the line of fire losses. Just following the general trend, when times are bad the losses go up, and when times are good the losses go down.

The CHAIRMAN: Then I think we will adjourn now.

The Commission adjourned at 5 o'clock until Thursday, April 19, 1945, at 10 a.m.

Canada Co-operative, Roy. Comm. R.

ROYAL COMMISSION
ON
CO-OPERATIVES

1945

PROCEEDINGS
(OFFICIAL REPORT)

VOLUME No. XXI

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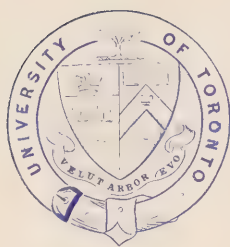


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T. S. HUBBARD
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ROYAL COMMISSION ON CO-OPERATIVES

Ottawa, Thursday, April 19, 1945

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ROYAL COMMISSION ON CO-OPERATIVES

The Commission appointed to inquire into the present position of Co-operatives in the matter of income and excess profits tax, organization and business methods and operations, and the comparative position of persons engaged in business directly competitive therewith, met in Ottawa, on Thursday, April 19, 1945.

PRESENT:

The Hon. Mr. Justice ERROL M. McDOUGALL, Chairman.

B. N. ARNASON	}	Commissioners.
G. A. ELLIOTT		
J. M. NADEAU		
J. J. VAUGHAN		

Eugene T. Parker, K.C.	}	Associate Counsel.
Roger Brossard, K.C.		

Major H. D. Woods	}	Associate Registrars.
J. A. Chapdelaine		

Colonel G. W. Ross	}	Executive Secretary.

APPEARANCES:

W. B. Francis	Group of Co-operative Associations	
W. H. Howard, K.C.	Private Grain Interests	
W. P. Fillmore, K.C.	Private Grain Interests	
R. H. Milliken, K.C.	Saskatchewan Co-operatives	
G. W. Mason, K.C.	American Reciprocal Association	
V. Evan Gray, K.C.	Factory Mutual Fire Insurance Companies	
Hon. S. A. Hayden, K.C.	American Mutual Alliance	
N. S. Robertson	Ontario Cash Mutuals	
Russell McKenzie, K.C.	Canadian Board of Marine Underwriters	
J. A. Mann, K.C.	}	Joint Stock Companies
Aime Geoffrion, K.C.		
A. Leslie Ham		

Ottawa,
Thursday,
April 19, 1945.

The Commission met at 10 a.m., Mr. Justice McDougall presiding.

MR. PARKER: Mr. Chairman, before we proceed this morning I should like to mention one matter of a general nature, and it is in relation to the argument of the so-called insurance groups. I think it is desirable, from the point of view of the Commission as well as of counsel engaged in this case, that some sort of decision be arrived at with regard, first, to whether they wish to submit their argument in writing at a later date, in which event they could take their time in the preparation of it, or whether they would prefer to make verbal argument. If they prefer to proceed with verbal argument, then we must give some consideration as to when. I am going to suggest that if some time during the day counsel for the insurance groups could get together and perhaps discuss it among themselves and make known to the Commission, through me, what their wishes in the matter are, we shall then do what we can to accommodate them.

THE CHAIRMAN: I think that would be a good idea; then we could discuss it at adjournment.

MR. PARKER: Yes, and have some sort of definite understanding about it -- if counsel would be good enough to do that.

We propose to take up this morning the Ontario Cash Mutuals, for whom Mr. Robertson is appearing.

Ontario Cash Mutuals

MR. ROBERTSON: Mr. Chairman and gentlemen, this is the presentation of the group known as the Ontario Cash Mutuals,

which, as you will see from the brief which has been filed, are The Gore District Mutual Fire Insurance Company; The Economical; The Waterloo Mutual, and The Perth. There are in Canada some additional cash mutuals which I am not representing. In the east there is the King's, the Pictou, and possibly another small one -- they are all small companies. In the west there is the Saskatchewan, the Portage la Prairie and the Wawanesa, who fall handily into the same category because they do business generally in the same way.

These Ontario Cash Mutuals are very old companies, as you will observe from page 1 of the brief. The Gore, for example, is over a hundred years old, having been incorporated in 1839. The Perth and the Waterloo go back to 1863 -- over seventy-five years.

THE CHAIRMAN: Where is the Gore District?

MR. ROBERTSON: Well, that is a rather interesting matter of geography. The Gore was a section that ran from Kitchener and Waterloo down in a gore shape towards Hamilton, and the name arose from the way in which the early surveyors started to lay it out. We have in the locality the Gore townships, and this territory was known as the Gore District. You will observe that the Gore was incorporated under 6 William IV originally; it operates at present under dominion registry and is incorporated by special act. In this connection the last paragraph on page 1 of the brief may be of interest:

"It is interesting to note the recital in the statute under which the Gore District was incorporated (6 William IV, cap. 18, 1836, carried over into the Consolidation of 1859 as cap. 52) which sets forth that 'Divers loyal subjects have by their petition represented the great advantages that would

arise from the introduction into this province of the principle of mutual insurance against losses by fire and prayed the interference of the legislature to enable them to bring the said principle into effective operation.'"

I should say on the instructions of my clients at the outset that while they have strenuous and serious objection to the application of a profits tax in any form to mutuals, on the ground that you cannot fit that kind of suit of clothes on that kind of individual -- they are a non-profit organization -- they are not in any way desirous of avoiding or evading bearing a fair and equitable share of taxation in this country; but it must be fair and it must be equitable. I should observe at this point that a profits tax generally is not the kind of tax that can apply to mutual operation. Of course that in some measure is begging the question. But may I make this observation in connection with an excess profits tax. Members of the Commission know and the public know that the purpose of excess profits tax legislation was to meet a war situation, a war which is just about over. It was intended to drain off those excess profits which trading organizations and individuals would enjoy as the result of war prosperity; and these remarks apply as well to the stock companies as they do to the tax mutuals. Insurance companies, with the possible exception of marine, do not sell merchandise to the government; there is no increase in volume of business as a result of war. So that the purpose of excess profits legislation so far as our excess profits tax is concerned does not obtain in connection with the cash mutuals.

Now, coming to my particular clients, the four Ontario Cash Mutuals, I pointed out their age, and I should like now to line up for you generally their method of operation. I

have observed a certain amount of mental verbal gymnastics as to the use of the term "surplus" amongst some of the submitters of briefs, and underwriting profit. At the outset let me say that these cash mutuals operate in a manner very similar to the joint stock companies. They have offices; they have office equipment; they have employees, and -- I hope that my use of handy language will not be turned against me -- they carry on a business in the ordinary connotation of that term. They have agents. They issue policies. They take applications, and generally they carry on similarly. They employ agents and they pay commissions. They solicit business. They issue contracts, and, like the stock companies, but possibly with greater happiness, they pay losses. They take and accept re-insurance. But there is a fundamental difference which shows itself all along the line in their operations. In the over-all picture their rates are less; their commissions are less, and there is no profit motive.

In connection with my particular clients, they are comparatively small companies. They originated in the early days as straight farm mutuals. By reason of the exigencies of business and competition they were forced to change their method of operation and became cash mutuals. They are very similar to life companies; and it is to be observed in connection with the brief of our friends the stock companies that they do not raise any issue as to life insurance companies -- the life field. We issue participating and non-participating policies, and must be distinguished from the farm mutuals, for example. The farm mutuals issue only participating policies. Certain life companies issue only participating policies, and certain life companies issue only non-participating policies; we issue two classes, the

participating policy and the non-participating policy. Our non-participating policy is our cash business, hence the name, cash mutual -- where we take a premium to start with on the issue of the policy and that policy holder has no further liability. Then we have our participating policy, which is on the old mutual or premium note basis, where we take a small payment with the application for the policy and a premium note for five times the initial payment. I want to draw that distinction to your attention.

Generally speaking we carry on the bulk of our business in southwestern Ontario. We have no association, for example; we do not need an association, because every head office is within twenty-five miles of the other. Perth is at Stratford; Economical and Waterloo are at Kitchener, and the Gore at Galt -- within a small compass.

Having grown out of farm mutuals the bulk of our business is on unprotected risks. We have for example 16,000 farm risks. I refer to this on page 2 of the brief -- and may I read just one paragraph:

"The four cash mutuals insure at least 16,000 farm risks as well as a large number of village, town and other risks which are not protected by municipal or other firefighting organizations. Many of the stock companies will not insure these unprotected risks and in cases where farm risks are accepted the rates are higher than those available from the mutuals."

Which I am going to establish; I am going to put Mr. McIntosh of the Gore in the box, and Mr. Foot of Economical.

I mentioned that we started as purely mutuals. The reason for that is shown on page 2 of the brief, the last paragraph:

"The broad shift from reliance on premium notes, payable in arrears, to cash premiums paid in advance was brought about by the stock companies. In entering the fire insurance field the stock companies approached the public with the cry that the mutual policy holder's liability was never fixed but was undetermined and unlimited, and that a mutual policy gave no security."

Now, we have heard a good deal about things that have been described in language that has come to us from the accountants -- surpluses, underwriting gain and loss. I do not think this Commission or this investigation should be fenced in, may I say, by any particular language, but I shall deal shortly with the question of surplus and the question of underwriting profit as these terms relate to the cash mutuals. If you will look at page 8 of the brief you will observe on that page a statement of the surpluses held by the four companies for whom I am appearing. I would direct attention to the quotation from the Ontario statutes governing these mutuals, commencing on page 7. In order to save the time of the Commission I will read only subsection 5 at the top of page 8 -- the other sections are there for the examination of the Commission:

"(5) The said fund may not be reduced by the payment of dividends to shareholders or members, or by a reduction of current premiums below the limit of 2 per cent of the insurance in force hereinbefore mentioned, but it may be increased beyond the said limit if the company so desires.

"The above statutory provision clearly indicates why the Ontario Cash Mutuals which over the years have accumulated large reserve funds are in such a strong financial position to-day."

Then I read from what I suppose is the third paragraph -- it is unnumbered:

"The following table shows the net amount of fire insurance under the policies of the cash mutuals at the end of December, 1944 --"

I may observe that the figures appearing in the brief, except this and the table at the very end of the brief, are for purposes of comparison taken from the last available dominion blue book, which at the time this brief was prepared was 1942, published in 1943. To continue, the amount of the respective surpluses of these companies at the end of December, 1944, was as follows:

	<u>"Net Insurance in Force</u>	<u>Surplus</u>
Gore District	\$123,415,863.	\$2,508,573.
Economical Mutual	114,057,549.	2,940,246.
Waterloo Mutual	83,690,151.	1,988,356.
Perth Mutual	46,982,771.	1,818,304."

Now, keeping in mind the fact that the statute requires us to average 2 per cent, it is to be noted -- this is reading from the next paragraph -- "that all of the companies hold reserve funds not greatly in excess of 2 per cent of the insurance in force." That refers to fire only, because that is what is affected by the statute. And the next sentence: "The proportion of the total reserves held for casualty insurance is in no case unreasonable in amount."

In connection with these reserves the Commission will please keep in mind the fact that these companies have been operating, in the case of Gore for over a hundred years and in the case of the others for seventy-five years, and these surpluses are the result of long years of operation, and are the result of prudent policy -- the policy required, may I say, of a trustee -- because I can conceive that these mutual

companies in our case are in no different position, notwithstanding the cloak of corporate entity, from that of a trustee of the policy holders' money. I will deal with the question of Salomon & Salomon and the other authorities, but I say that this Commission must look through the mere legal rules and regulations; the body to consider Salomon & Salomon and the other authorities is the Exchequer Court. This Commission is considering the public interest, and in connection with that may I press upon the Commission that the cash mutual companies are merely trustees to receive and administer and disburse and husband the policy holders' money.

Now, we have had a great deal of discussion as to reserves and surplus -- I care not what you call them for the purposes of the present inquiry, and I do not propose to recultivate the ground that has been so well tilled on the general subject of surplus and reserve; I do not think anything I could add would assist the Commission beyond what Mr. Gruhn has said, and Mr. Gray and others who have spoken. Let us consider underwriting profit -- keeping in mind again what I have just said with regard to the position of the cash mutual being essentially that of trustee. I should like to read for emphasis, as I assume the whole brief is available to and will be examined by the Commission, the first portion of page 6:

"'Underwriting profit' (and loss), a term widely used in insurance literature, means only the excess of premium income over losses and expenses. As applied to a cash mutual company it means only that its amount is available to reduce future premiums or meet future losses. In contrast with a stock company the term 'underwriting profit' means that the management has added a profit to the stockholders' account from which in the current or future years dividends can be paid

to stockholders. In the case of stock companies it has no relationship whatever to present or future cost of insurance; if not immediately disbursed as dividends it may go to reserve, there to be the property of the shareholders, not the policy holders, and while it may contribute to the security of policy holders it is a protection to the stockholder's invested capital and is a profit thereon and as such is and should be taxable.

"The above distinction is well recognized in income tax law."

If this is the proper tribunal to consider the legal aspects of this matter.

"The principle has been stated to be that income tax charges what goes into the taxpayer's pocket and not on what his pocket is saved."

In the case of the mutuals the money is not going into the policy holder's pocket; his pocket is being saved. In contradistinction, and dealing with the shareholder's interest in a stock company, the money is going into his pocket. It is income to him. His pocket is not being saved, except in the other character that he may take a policy with his own company, where then he saves on a reduction basis, but in the character of a shareholder he is getting a profit. While my friends the stock companies have drawn in their brief a beautiful analogy, beautifully stated, between stock and mutuals, they have overlooked the essential difference of the profit element, which I submit and press upon this Commission is the essential thing in determining whether it is in the public interest or not.

THE CHAIRMAN: The argument is that his patrimony has been increased by the amount of the saving, and to that extent

it is profit.

MR. ROBERTSON: That is just my point, Mr. Chairman. That is not an element that can be taxed under any principle of income tax. It is not that his pocket is saved; it is what goes into his pocket. That principle was applied in the Montreal Coke case. The argument there was that the company was saved over the years a difference in interest on the refinancing of the bonds. They struggled manfully right through to the Privy Council, and that was the principle referred to there by the committee, and referred to in argument -- that it is not what is taxable --with all respect, I should not be arguing this; it is a legal matter, but it is what goes into the pocket, not what is saved the pocket, that is taxable. I say that is relevant to this situation; that in a mutual company it is altogether savings; in a stock company it is altogether profit. To continue:

"In the case of the mutuals the 'underwriting profit' saves the pocket of the mutual policy holder something on his current or future insurance cost whereas in the case of stock companies the underwriting profit goes into the pocket of the stockholder. Reference is here again made to the enormous sum of over \$42,000,000 paid in dividends by Canadian stock companies since 1875 as above mentioned."

Then referring to page 3 of the brief, the third last paragraph, I read:

"To provide security the mutuals as their business has increased have built up reserves against conflagration and contingency and at the same time have constantly reduced their rates as conditions warranted. On the other hand stock companies while seeking to set up adequate reserves strive to make profits for their shareholders. That stock companies have been successful in their endeavours to make profit is established from p. xviii, vol. 1 of the 1942 report of the superintendent of insurance where it appears that since 1875 down to 1942 (inclusive) Canadian stock companies had paid dividends to their shareholders of \$42,395,000 and in the year 1942 alone the stock companies paid \$1,479,000 in which year they enjoyed only 36 per cent of the premium income."

Since this brief was written we received the following Year Book; and in the year 1943, the figures for which were not in the table I gave on page 3, the stock companies paid \$1,509,672, or \$30,000 more than they paid in 1942; and they filed a brief complaining that they are being hardly treated; and they adopt the taxpayers' association brief. I submit the figures do not show that they are being badly treated. Now I continue reading on page 6, where I refer again to the life insurance analogy:

"Indeed analogous situation exists in respect of life insurance companies. They possess large investments from which they derive income."

And may I interject here that in the brief of the stock companies they accept the life field. I just want to emphasize that; that is, the life companies.

"They possess large investments from which they derive income. The investment income is an essential element in the determination of their rates. As the interest rate goes down the cost of insurance goes up, as has happened recently because of the current trend of interest rates to the lower levels."

So the interest rates are an essential element in the rate-fixing of any life insurance company, and I submit they are in the fire insurance field.

Now, speaking of the investment income, there has been a great deal of discussion of that. My submission to this Commission is that in the case of the mutual company, as I mentioned a few moments ago, the position of that company is that of trustee, nothing more and nothing less. You will say a trustee is taxable. Certainly he is; a stock company trustee is taxable. If somebody dies and appoints a trust company as trustee, the trust company goes to the court and is awarded compensation, and pays a tax. Why? Because the stockholders of the trust company are in that business for a profit. But let us examine what happens to the moneys that trustee gets in for his trust, for his beneficiary. If he is the trustee of my estate, and he gets in interest, is he, the trustee, taxable on that interest? No, he is not. He is only a trustee for it. He passes it out to my heirs, if I have any. He is not taxable on that income; and I say that in the case of the mutual companies.

On the other hand he is taxable on the compensation, that is his profit; but he is not taxable in what he gathers in for his beneficiaries. He gathers it in from the estate, and pays it out; and in my submission you have an exact analogy in the case of cash mutuals. In our case we gather in our investment income, and it is held and applied in the

reduction of rates, and increasing our security; because our business may grow, or because in the case of the cash mutuals, for example taking the Dominion Blue Book, we carry -- that is, these clients now making their submission to you -- twenty-five per cent of the wind insurance recorded in the Dominion Blue Book. In the case of the Economical, this is carried in four or five counties in Ontario. Fortunately we do not have the extremes of windy weather that they get other places. It could happen, however. We could have a serious loss. Therefore we must have a reserve, and we must pass our interest earnings, underwriting gain and other moneys to that security.

To come back for a moment to the analogy I have just drawn between a trustee in the case of a stock company and a trustee in the case of a mutual; in the stock company the trustee is in the position of the trustee trust corporation, where the shareholders get the compensation as their profit. And indeed the fire company, the stock fire company or the stock life company, are in the same position. It has been intimated here in that case that in any of your fire companies you have a large reservoir of funds which come in from others, the stockholders, who are not policyholders. In the case of the stock company, the stockholders cream off the top of the can the profits for themselves, as the corporation trustee does. But in the case of the cash mutuals you have nothing of that kind, because there is nobody there to get it.

Again, in respect to your invested income, I could apply my remarks to that, because there is no point in my re-canvassing the different aspects of whether it is income or whether it is not. Mr. Gruhn has done much better than I could hope to do in that connection.

Now let me just make this remark at this point; that it will be observed in connection with the stock companies that they are saying to you gentlemen, "Find that the cash mutuals have a profit, because it looks like a profit and they call it a profit." Surely you must look through that and see where that money goes. Calling it a profit; calling it an underwriting gain, calling it investment income, does not make it such unless you follow it through. As I mentioned a while ago, we are in the framework of accountants' language. That is all right when you come before a judicial body who are construing the statute; but this Commission has to determine whether the taxing statute should be applied; and I submit that they should look through mere language and go beyond it.

I want to point out something else in respect of the analogy between life companies and fire companies. There has been a good deal said about what happens to the part of a mutual policyholder's premium which has through surplus for reserve, when he drops out; and it has been suggested that that is a profit, in some way; that that little portion of his premium, when he ceases to be a member, which during his tenure of membership from year to year, while he was in, had gone to the reserve was a profit and should be reached by the taxing statute, or may be within that category which this Commission is to say should be reached. But what happens in a case of a life company? You have lapses. Has anybody suggested that after a man has carried a life policy for four years and has paid premiums, and for one reason or another, disinterest, financial inability or otherwise, he does not continue to carry it, so that the life company has four premiums -- is that profit? I submit not, because he was required to pay that to carry the risk, that intangible thing "risk"; and I submit in fire insurance

it is the same.

Take the case of the surrender of a life policy. That man does not get back all his money; and I think this is a very close analogy. A man pays in premiums for ten years. At the end of ten years he elects to surrender his policy. Does the company give him back his money with interest? No. You have a table in the back of your policy showing the surrender value after ten years to be X-dollars, which is the total of what he has put in less something. What is that something? It is the risk. It is intangible. You cannot pick it out of the air; you cannot put it in a box and hold it up for inspection, but it is still what he paid for. I submit to the commission that what has gone of a mutual fire policyholder's premium into reserve contains the element of having paid for the risk.

Then, again, when he came in he got security, because there was then, particularly in our old companies, an accumulated reserve which he did not pay for but which carried his risk. When he came in he paid \$10; let us take an even figure. If the company were starting at that date the \$10 would not have taken care of the risk and given the security. But he steps in with a \$10 premium, a low premium, which he can do because of perhaps a hundred years of careful operation.

Then he steps out. It is true that if he has been there for three years, each year probably something has gone to reserve, be it out of underwriting gain or so-called investment income. It is suggested that they keep something away from him which is not a cost; that they keep something away from him and it is therefore profit. I submit it is not profit. He is then paying, when he goes out, for that thing he got when he came in; that is, security, and it is the element of paying for the risk.

Now let us examine the underwriting profit feature of mutual operation from another aspect. I know what my learned friends are going to say about Salomon and Salomon, but just let us suppose now that Mr. Foot, who is manager of the Economical, by some magic becomes the Economical. He is the Economical. Let us forget for a moment the interposition of this legal entity, the company. He is now carrying on the business; he takes in the money from the mutual policyholders; he pays the losses, arranges the reinsurance, and so on. Let us say this Mr. Foot, the individual, has become the Economical mutual. What part of the money that passes through his hands at the end of the year is taxable? His salary, and only his salary. Is the investment income that Mr. Foot has been handling, that he has been taking in and seeing is paid, and putting in the bank -- is that taxable in Mr. Foot's hands? I submit not.

THE CHAIRMAN: You are supporting the reciprocal case, then?

MR. ROBERTSON: Yes. I am saying, Mr. Chairman, that in the case of the cash mutuals or any other mutuals, you have an agency. It is true that you may tax an agency on its profit. What does Mr. Foot get out of it? He gets a salary, the same salary that he now receives; no more and no less. He pays his tax on that salary, but he does not pay anything on the underwriting gain or loss; that is his policyholders'. You have hit the nail right on the head. The position is not different, by reason of the interposition of the company.

Our friends will say "Yes, it is, because the taxing statute taxes the company. You must screen it off where the company is, and catch the tax there." That again, of course, is an argument for the Exchequer court, but I think it is

pertinent here.

But look at what the statute does in that case. What does it say about a personal corporation? This is the other side of the shield, you see. What does it say about a personal corporation? It does not say, in reference to a personal corporation, that the profits or earnings of that corporation will be taxed in the company. It states right through that it is the individual. Where is it different here, where you have a non-profit organization? Your statute recognizes the individual shareholder in the case of a personal corporation; it goes right through it. You will find it in section 21 of the Income War Tax Act, which I might read. This is just on the point that the argument that there is a corporate entity does not really hold water when you examine it with the statute. Look at subsection (1) of section 21:

"The income of a personal corporation, whether the same is actually distributed or not, shall be deemed to be distributed on the last day of each year as a dividend to the shareholders, and the said shareholders shall be taxable each year as if the same had been distributed in the proportions hereinafter mentioned."

You get the legal fiction of a corporation, and therefore it must be taxed. That is a statement which is completely destroyed by the provisions of the present act, where they go right through the cloak of corporate entity. But I pointed out to you what happens in the case of Mr. Foot, supposing he is the Economical. Nothing that comes in, in the way of underwriting gain or investment income or anything of that kind, is taxable in his hands. But now let us put Mr. Hurry of the Northern Insurance Company in the same position. Supposing the Northern Insurance Company

is Mr. A. Hurry, carrying on business as the Northern Insurance Company, and what happens to the investment income in that case? What happens to the underwriting gain in that case? He is taxable; there is a difference, I submit. In the one case of the mutual company you just reach through this thing and see what actually happens, regardless of the form, regardless of the accountants' language, regardless of corporate entity; you see what actually happens, and I submit in the analogy it clarifies the position.

In Mr. Hurry's case, the case of the stock company, you have Mr. Hurry having to pay all the taxes because he is the proprietor, and he makes the profit. He is there to make a profit, and more power to him. There is no criticism on our part of profit-making. All we say is that it is absent here. If there must be a tax, we submit that the tax as related to the mutuals is not to be a profits tax, an income tax or excess profits tax.

Further on the point of underwriting profit and investment income and the like, I do not think we need go beyond what Mr. Gruhn has said. He is a man of very broad experience, and I cannot add anything to his statement.

There is another aspect of this matter to which I should like to refer; that is the order in council. I should like to indicate just some of the provisions and apply those provisions to what I have to say. The commission, under (a) is to inquire into the personal position of cooperatives; and I greatly regret that the mutual insurance people should be mixed up with cooperatives at the moment in this investigation. Under (b) it is to investigate the organization and business methods of the cooperatives, and any other matters relevant. Then the commission is to report all facts which appear to be pertinent for determining what would, in the public interest, constitute a just, fair and equitable

basis for the application of these statutes and for the amendment of existing laws.

I submit that there are really two aspects of public interest. One is the interest of John Citizen in two characteristics, one as a taxpayer and the other as a plain citizen. The other is the public interest of the treasury, in revenue. Let us deal for a moment with the interest of the treasury; let us see what our friends, the stock companies propose. I would refer you to this yellow brief filed on whose behalf we do not know as yet. We know Mr. Geoffrion, Mr. Mann and Mr. Ham, but we do not know who is really speaking; it has a certain anonymity about it to date, though we hope to clear that up later. Let us look at page 11 of their brief.

THE CHAIRMAN: Which brief; the supplementary brief or the main one?

MR. ROBERTSON: No, the first brief. They propose and suggest in clause (a) that all exemptions from taxation with respect to insurers in the other than life field be eliminated. That is, as Mr. Gray has so well pointed out, that they want section 4(g) out of there; and, as he pointed out, section 4(g) was simply a statement of the common law.

Then they deal with Mr. Mason's clients, the reciprocals, and then they come down to paragraph (c). I would not comment upon the clarity of paragraph (c) or its meaning, but I think I know what it means. Let us read it:

"that the recognition by parliament that reciprocals and mutuals enjoy an advantage over the stock companies appearing from the differentiations in the premium tax enacted by . . . , the special war revenue act. . . be eliminated as being in no wise an equalizing measure and consequently that such sections be repealed;"

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In case we get some objections from the back seats, I will read the last phrase in a moment. What they are proposing down to the semicolon, however, is the repeal of the premium tax. I cannot read any other meaning into it. Then they go on and say, "or make it even," and that is just what we say. We say if you do not repeal it, make it not two per cent for the stock companies and three per cent for us and four per cent for the reciprocals, but make it even. But let us leave out the last phrase and see what they propose, down to the semicolon.

In the first place, we have had a great deal of discussion about profits and a profit tax, but as yet no one has mentioned any figures. If you will look at page 14 of the cash mutuals' brief, we have given you some figures out of the Blue Book. We have substituted new pages 14 and 15; the arithmetic in the original pages was not too good, but it does not change the argument in the slightest. The error in arithmetic hurt ourselves, because we took off too much. Now let us look at the corrected figures on page 14. You will see that from the Blue Book, the second item in the right hand column, the cash mutuals had total net premiums of \$4,438,803, on which we paid three per cent. That would give a tax of \$133,164. These figures do not appear anywhere in the brief, if you wish to take them down. Three per cent on the premium income of the cash mutuals, that is the special war revenue tax, would be \$133,164. Then you take the Alliance group, which is the other mutuals, and you have the second last figure from the bottom, \$4,490,034, at four per cent, which yields roughly \$175,000. Then you have the stock companies and the others bulked, paying two per cent on \$86,000,000. So that you have, at your present rates of two per cent, three per cent and

four per cent, the treasury now receiving \$1,952,000.

Again going back to the stock company brief, in paragraph (c) they propose -- leaving out the last phrase again -- that that be eliminated; that the treasury lose that amount. That is what they propose in paragraph (c).

Now let us see what they propose to give the treasury in (a), and I should say that these figures are not final; but I suggest and recommend that Mr. Glassco prepare final figures to carry out the idea that I am expressing. I was limited to those figures which were easily available, and I have proposed to apply to the mutuals, so far as I can, the income and excess profits taxes, so when the stock companies take away the \$1,952,000, let us see what they propose to give back.

In the case of the Economical, Gore, Perth, Waterloo, Wawanesa, Portage and Saskatchewan, that is the cash mutual group leaving out the Kings and the Picton, which do not amount to very much, and taking the standard profit as the average of the figures that appear in Stone & Cox as a convenient place to get it, in some cases we took a two-year average instead of four years, the standard period being 1936 to 1939, but this can be worked out from the Blue Books. You have this situation. You have the cash mutuals paying in income and excess profits tax some \$598,000. You have the Alliance group -- and the figures for that are from appendix IV, the recapitulation of the Alliance group brief -- you have the underwriting profit there, and you have the profit for 1943, so that you have for the Alliance group, apparently, \$118,000. There were no figures readily available for the Manufacturers or the reciprocals, but you have from both cash mutuals and the Alliance an income and excess profits tax of \$717,000. So you would have to gather in from the

Manufacturers group or possibly investment income, in the case of the Alliance group, because I cannot tell that this is only underwriting gain -- the difference between \$717,000 and \$1,952,000, which is \$1,200,000, before the treasury would be as well off as it is now, if you accept what they propose here.

That is the first point of public interest. Is it in the public interest to adopt what our friends suggest; that is, the elimination of the premium tax, and impose instead the profits tax? I submit that it is not, from that aspect.

There are other matters of public interest; and I would just wish to refer again to the language of the order in council:

"-- on what, in the public interest, constitute a just , fair and equitable basis for the application of the Income War Tax Act to the mutuals."

So what is the basis that is to be just, fair and equitable? Having that in mind, and continuing on the matter of public interest, I would like to refer the commission to pages 16 and 18 of our brief. That is the section headed, "British and foreign stock companies enjoy a further peculiar tax preference by avoidance of tax on investment income."

You will observe that in the first paragraph, which we have taken from the 1942 Finlayson Report at page 68, we have the division of the Canadian field. I will not trouble to read page 16; it is there for the information of the commission. The point is that the large portion of the premium payments of Canadian citizens go to foreign companies to which, under the income and excess profits tax acts, the charging sections as far as earned income is concerned, do not apply.

Take a British company doing business out here. It

drains off a substantial portion of the Canadian citizen's insurance dollar. That money goes out of Canada; possibly it is invested in Canada. The security is taken out of Canada to the head office, "notionally," only. Mark that; it is taken out notionally only; Mr. Finlayson requires it to be kept here, and it earns interest here, but it is not brought into account for the purpose of tax. In this connection I should like to read from page 17:

"The interest earnings of most of the foreign and British Companies, as shown in the superintendent's report, bears no relationship to the interest on the value of bonds and debentures on deposit with the Receiver General. The following are examples; the Commercial Union, page 191, 1942 report, held on deposit with the Receiver General - \$932,594.20."

That is a sizable chunk of money.

"--interest earned - \$2,772.00; The Helvetia Swiss, page 353, held on deposit with the Receiver General - \$167,608.00, interest earned \$750.00; The Royal Exchange page 647, held on deposit with the Receiver General - \$864,656.00, interest earned - nil; Pearl Assurance, page 582, held on deposit with the Receiver General \$803,584.00, interest earned \$6,721.50."

These companies are not bringing into Canada these large sums of money from foreign business. Mr. Finlayson surely is not asking them to bring in money from the United States or England. This is money which had its origin and was derived in Canada.

"Looking at the tables on pp. cxiv to cxxv of the 1942 report we find the income in Canada of the different classes of company, taking the totals of the column headed "Income, rents and dividends on stocks earned"-

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<u>"Canadian companies</u>	<u>British companies</u>	<u>Foreign companies</u>
3,408,274	860,786	1,097,553

but as appears from p. lxii (table B) and p.xx (2nd table) of the 1942 report the several classes of companies enjoyed the Canadian business in 1942 in the following proportions:

<u>Canadian (including British and Foreign controlled</u>	<u>British</u>	<u>Foreign</u>
<u>Fire Casualty</u>		
12,636,228 (26.23%)	16,394,902 (34.03%)	19,140,329 (39.74%)
17,163,984 (34.1%)	12,642,254 (25.2%)	20,328,965 (40.7%)
29 ,790,212 (30.3%)	29,036,156 (29.3%)	39,469,294 (40.4%)

It is to be observed that Canadian companies enjoying only 30.3% of the total business have all their investment income \$3,408,274, included in profits for tax purposes while British and foreign companies enjoying 69.7% of the total business earn only \$1,958,339 investment income in Canada and this is not included in profits for tax purposes."

Can it be said to be just, fair and equitable to apply a profits tax to a non-profit organization when you have a situation like that? In connection with the application of the tax to British and foreign companies, and to marine insurance, with which I will deal in a moment, you heard what Mr. Hayden had to say. I had hoped that an income tax official would have been called, so we could clear this up. My information has come from the insurance department unofficially; I have been so advised, that this income is not caught, and I would suggest that a tax official be called to clear this up.

I may be wrong, though I do not think I am. There is only one way of finding that out, and that is by calling a tax official.

Now I read at the top of page 18:

"We submit the above clearly establishes the inequitable incidence of income and excess profits taxes whereby the Canadian stock companies are caught and bear the burden of taxation and British and foreign companies enjoying over two-thirds the business escape. In no case, except in the case of Canadian incorporated companies, does the interest from investments form a part of the taxable income.

"It will be observed that the inequitable incidence of income and excess profits tax arises from the difference between the manner of computing 'income' to which to apply tax against Canadian stock companies and the manner of computing the 'income' of British and foreign companies and this inequity should be remedied.

"What happens is that 'income' of Canadian companies includes the income received from the investment of its capital reserves and unearned premium as well as its so-called 'underwriting' profit. In contrast in the case of British and foreign companies very little (if any) investment income is so included as taxable income on the theory or fiction that the investment income of a company having its head office out of Canada is received at the head office out of Canada and as it is supposed to pay the head office expenses referable to Canadian business it is not to be included in the income of the company for the purpose of income and excess profits taxes."

I may observe, and I suggest that this should be ratified by calling a tax official, that this practice arose, I think

back in 1933, or about that date, when the invested income on deposits was then said or decided to be considered as equivalent to the expense applicable to Canada incurred at foreign head offices; and I suggest that is a point which should be cleared up. Just in contrast with that situation, and along the line of some discussion that has taken place as to the desirability of imposing tax on investment income, I should like to read the second paragraph on page 19 of our brief:

"The application of the Income Tax Act and the Excess Profit Tax Act bears little relationship in so far as Canadian companies are concerned to the underwriting profits and, as pointed out above, a number of Canadian stock companies have paid in the form of income tax and excess profits tax considerably more than the underwriting profits made by these companies."

The reason, of course, being that the underwriting gain is small and the accumulation, for example in the Western, over those years of operation is large.

However, taking into consideration the most extreme stock company cases, it would not compare with the application of these acts to cash mutuals, where in 1942 the four cash mutuals made an underwriting gain--"

I am referring back for the moment to page 8, where the sum of insurance in force is shown at about \$400,000,000; and they made an underwriting gain --

"--of \$77,531, their income from reserves was \$390,475, or a total of \$468,006. The minimum payable on this income based on forty per cent would have amounted to \$187,202 or approximately 250 per cent of the underwriting gains for that year."

So it does not seem that it should be applied. Would it be

just, fair and equitable to apply a profits tax on any basis to mutual, non-profits activities while you have the very companies that compete with us enjoying large profits from marine business, which apparently again completely escapes taxation? Just let us look at one company as we go along. I deal with that at page 13 of the brief; but before going on with that point, just let us look at the Blue Book. I am reading from the 1943 edition, at page 212. This is the Continental. If you will look at the statement of the Continental appearing in the 1943 Blue Book, starting on page 210 and continuing over to page 212, I should like to just read into the record what happens in connection with this company's marine business. The net premiums written amounted to \$408,643. The losses incurred totalled \$18,326. The expenses and taxes incurred amounted to \$86,000. The underwriting gain was \$389,254. They made an underwriting profit on their other activities of \$63,226; they made an underwriting gain on their marine business of \$389,000, which marine profit escaped tax. Now I should like to read on page 13 of my brief:

"Marine Exemption

"The marine premiums on business in Canada in 1942 (p.c.c. of 1942 Report) was as follows:

Canadian companies	\$ 563,493.	
British companies	6,680,367.	
Foreign companies	<u>7,050,716.</u>	\$14,294,576.

So we have \$14,294,576. stock company marine premium income which totally escapes the premium tax."

That is the first point, under the Special War Revenue Act.

"--Of this the large portion goes into the coffers of non-Canadian companies.

"The figures as to assets in Canada for marine protection are even more startling. For example, the Eagle Star collected in 1942 (p. c.c. of 1944 report) \$1,131,314. in premiums against which it held assets of \$17,543 only and the Sun Assurance enjoyed a premium income of \$1,033,270 but had no assets in Canada in respect of marine business. It is also observed that no company doing marine business in Canada received in Canada any income other than premium income except the Hartford which reported \$2,121, other income. Taking the totals for British and foreign companies only we have total premium income in Canada for marine business of \$13,731,083, total losses in Canada and other expenses in Canada of \$9,514,753 (\$7,576,384 plus \$1,938,369) which deducted from the total premium leaves \$4,216,330 excess, as a net premium income apparently siphoned out of Canada which bears no premium tax, income or excess profits tax."

The corresponding figure, extracted from the 1943 book, is \$3,073,046. That is not in the brief. Those figures will be found in the 1943 report, the last ones at page 82, I think it is; I am not very sure of my Roman numerals. The figures in the mimeographed brief were taken from the 1942 book.

"Furthermore, most of these non-Canadian companies writing marine insurance and enjoying this preference as to premium tax also write fire and in many cases casualty insurance directly and through Canadian subsidiaries."

These are the people who, in the income tax payers' brief, and in their own brief, are heard to say that they are badly treated, competition-wise. They compete with us in the fire and casualty business; and the same companies carry on marine insurance, in which they escape this taxation.

"Besides the marine premium tax preference they

The first part of the paper is devoted to a general discussion of the problem. It is shown that the problem is of great importance in the theory of the structure of matter. The second part of the paper is devoted to a detailed analysis of the problem. It is shown that the problem is of great importance in the theory of the structure of matter. The third part of the paper is devoted to a detailed analysis of the problem. It is shown that the problem is of great importance in the theory of the structure of matter. The fourth part of the paper is devoted to a detailed analysis of the problem. It is shown that the problem is of great importance in the theory of the structure of matter. The fifth part of the paper is devoted to a detailed analysis of the problem. It is shown that the problem is of great importance in the theory of the structure of matter. The sixth part of the paper is devoted to a detailed analysis of the problem. It is shown that the problem is of great importance in the theory of the structure of matter. The seventh part of the paper is devoted to a detailed analysis of the problem. It is shown that the problem is of great importance in the theory of the structure of matter. The eighth part of the paper is devoted to a detailed analysis of the problem. It is shown that the problem is of great importance in the theory of the structure of matter. The ninth part of the paper is devoted to a detailed analysis of the problem. It is shown that the problem is of great importance in the theory of the structure of matter. The tenth part of the paper is devoted to a detailed analysis of the problem. It is shown that the problem is of great importance in the theory of the structure of matter.

also enjoy special advantages in the way of escaping income and excess profits tax on investment income under the fiction that such investment income is earned at a head office outside of Canada as will hereinafter be discussed."

I submit that it would not be fair or just or equitable to apply a profit tax to a non-profit organization, when you have such inconsistencies and exceptions as those existing in the tax structure. That is entirely beside the application of a profits tax to a non-profit organization.

The other matter bearing on justice, fairness and equity, again in the public interest, is the preference available to the stock companies, both local and foreign, with which I deal at page 15 of the brief, commencing with the third paragraph from the top of the page:

"A preference of two per cent on \$82,184,407 is equivalent to a tax saving of \$1,643,688 to the stock companies over foreign mutuals and reciprocals and a preference of one per cent over cash mutuals is a saving of \$821,844."

That is a saving to the stock companies.

"Now let us examine table A on p. ixvii of the 1942 report. We see here that the total income tax paid by stock companies amounted to \$1,619,458, a figure not materially different from the preference in rate that they saved as against their competitors under the Special War Revenue Act.

"Admittedly they pay \$2,733,455 under the Excess Profits Tax Act. But why should they not be liable to excess profits tax? They are in business to make profit (as contrasted with the mutuals) and should not be treated differently from any other profit-seeking organization

under the tax laws.

"The Canadian stock companies have not suffered--" Regardless of their complaint.

"--as is evident from the totals on p. xcix of the 1942 report where it appears that the total assets in 1941 were \$99,285,379, and had increased in 1942 to \$104,438,721 in spite of wartime taxes to which the stock companies were subject. The totals for Canadian companies on p. cvii of the report confirm this because they show that while the capital stock had decreased some \$96,000--" You will observe that the capital stock went down.

"--the excess of assets over liabilities (excluding capital stock) had increased by \$2,083,365 (\$61,468,974 less \$59,385,609.)"

So we have no great harm being done to the stock companies, competition-wise, according to the figures. Their feelings may be hurt by the mutuals, but certainly their pocketbook is not.

The remarks I have just made have had reference to the public interest from the point of view of the treasury, and as applied to the submission to this commission, to find what is fair, just and equitable in the application of these profit taxes to a non-profit organization. There is another phase of public interest. What about John Citizen as a **taxpayer**, and as an insured? Is it desirable, is it in the public interest that greater burdens be placed on the mutual companies which admittedly are a thorn in the flesh of the stock companies, and whose rates are admittedly lower than those of the stock companies, that is over the broad field? Is it in the public interest to place greater burdens upon those non-profit organizations, who are now paying a higher rate under the Special War Revenue Act? I submit that it is not.

I submit that it is very healthy that the mutuals, particularly the cash mutuals, who I have said carry on business almost in the same way, but for the profit motive, should be allowed to stay in the field and keep down the rates.

There is another very, very important phase of the public interest, in the aspect of the interest of the citizen. I refer to protection in the same general field as that in which the farm mutuals operate. The field of the cash mutuals and mutuals generally is the unprotected areas; that is, where they have not elaborate red fire engines, hose and fire-fighting apparatus. I pointed out earlier in my remarks to you, Mr. Chairman, that our people operate in that field; and I am speaking now at the moment for the four Ontario cash mutuals; I do not know what Wawanesa, Saskatchewan, or Portage la Prairie do. They may be operating only where there is fire protection, though I doubt it. The bulk of our business, not all of it but the bulk of our business, taking the four cash mutuals in a group, is in unprotected areas. We have said in the brief that we go into these areas and the stock companies do not. Mr. Foot will be in the box in a moment, and that question can be asked him. But let me refer you to page 35 of the brief. This is the agency registration plan, part of the appendix. I just want to point out one feature of the classification of the agents, for this commission, notwithstanding salary control and wages control. How they ever got over this, I do not know; but it may be outside the act. I quote:

"An agent already giving companies members of the C.U.A. . . not less than 50 per cent of his total fire premiums, excluding farms -- "

MR. PARKER: This is a quotation you are reading now, is it?

MR. ROBERTSON: Yes.

MR. PARKER: It was contained in a public address?

MR. ROBERTSON: Yes.

MR. PARKER: I just wanted to know the authority for it.

MR. ROBERTSON: It was a public address. It is not part of the brief. If necessary I think I can produce the authority. It is not very important, but I just point out that it does exclude the farms, both in the first paragraph and in the next paragraph, which is (b).

I say it is in the public interest not to put a profit tax on a non-profit organization which furnishes a part of the community needing fire insurance with that fire insurance at a low rate, where the stock companies do not want to go in.

I have not developed the competition angle in the remarks I have made, but it is there in the brief for all who run to read if they wish. In connection with this matter now being canvassed, I would recommend to the board that they look at page 45 of the brief, which is taken from the report of Judge Masten. May I read just the first paragraph; and remember that this is taken from the report of Mr. Justice Masten at pages 31 and 32.

MR. HAM: Was this evidence before the commission? It was not the commissioner's report? It was evidence before the commission, was it?

MR. ROBERTSON: The first part is the commissioner's words; those are paragraphs 2 and 3. The next paragraph, 4, is the evidence before that commission. The evidence is not taken by me from the sworn transcript; it is taken from the report of Mr. Justice Masten:

"It also appeared before me in evidence that a short time ago the tariff companies, under the name of The All Canada Insurance Federation, approached the Minister of

Finance at Ottawa, to request that the federal government should impose a tax on unlicensed insurance.

I add for your information certain extracts from the evidence of the general manager of the insurance department of the Canadian Manufacturers Association, which summarizes the arguments against the imposition of the suggested tax."

I think that clears up the point raised by Mr. Ham. I have the Masten report here if it is desired. Now I should like to refer to pages 22, 23 and 24 of the report, which I propose to read, and then I am through.

THE CHAIRMAN: Has a copy of the Masten report been filed already? I understand that we are getting a copy of it, but have not got it yet. Have you a spare copy?

MR. ROBERTSON: I have my copy here, and I shall be glad to leave it with you. You may have difficulty getting it. You will be able to get the Hodgins report, but I think I got almost the last copy of the Masten report.

Now I should like to read the part of my brief dealing with conclusions and submissions, beginning on page 22, and then I am done and will call the witness:

"The Ontario cash mutuals have no wish to avoid bearing their fair and equitable share of national taxes." But we are unalterably opposed to the kind of machinery which is proposed, to put on us a profits tax.

"However, the cash mutuals submit that regardless of legalistic arguments based on English tax legislation which differs materially from existing Canadian tax legislation or based on English decisions interpreting English legislation, a profits tax of its very nature has no application to their activities. It is further submitted that before any attempt is made to apply

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1. The first part of the paper is devoted to a review of the literature on the topic of the effect of the environment on the development of the individual. It is found that the environment has a significant influence on the development of the individual, and that the influence is both direct and indirect. The direct influence is through the physical environment, and the indirect influence is through the social environment. The physical environment includes factors such as climate, geography, and natural resources. The social environment includes factors such as culture, religion, and social structure. The indirect influence is through the social environment, which shapes the physical environment. The social environment also shapes the individual's development through the transmission of values, norms, and customs. The individual's development is also shaped by the physical environment, which provides the resources and conditions for growth and development. The physical environment also shapes the individual's development through the transmission of values, norms, and customs. The individual's development is also shaped by the physical environment, which provides the resources and conditions for growth and development.

profit taxes to mutual insurance operations the apparent glaring inequities in the present tax structure applicable to insurance should be remedied."

Apparently that is the view of the stock companies, as appears by the last phrase in paragraph (c) of their brief, to which I referred earlier. You will remember that I pointed out that they propose to take away the premium tax and give back the profits tax, but it would not equalize.

"The remedy of these inequities would be in the public interest because this type of tax would bear evenly on the whole fire and casualty business and would reflect itself to the same extent in all premium rates charged the insuring public."

Just there might I observe that there has been a discussion as to taxes, income taxes and profit taxes, filtering their way through to the premium. That may be in a measure; I am not an economist, and I would not argue that. But there is no doubt that if it is a straight premium tax it goes direct,

"If these views are adopted the public interest would no doubt be served in the way of increased income to the treasury.

"It is the opinion of the cash mutuals that the preference now enjoyed by British and foreign stock companies whereby the bulk of their investment income escapes liability for tax, should be eliminated. It is suggested that the remedy could be provided by legislation which would include in the taxable profits of British and foreign stock companies an item for investment income. It is suggested that the remedy could be provided by legislation which would lay down a rule for the determination of the amount of investment income

of British and foreign companies that would be brought into account for taxation purposes and such legislation in order to do equity should apply the same rule in respect of the amount of the investment income of Canadian companies made liable to tax."

The general differential is that the Canadian company, living here, is caught for everything, while the foreign company escapes. In fact my brief is partly a brief for the Canadian stock companies, not only the cash mutuals.

"Such a provision would make for equality of treatment and the Canadian companies would not be penalized in the way of having all their income from investments accumulated over the years made liable to tax as contrasted with the situation obtaining in respect to British and foreign companies who over the years have earned profits in Canada on Canadian business and have withdrawn these profits and the investments representing these profits out of Canada to their home offices so that under the present tax framework the income on past years' profits to-day escape tax because they are not in Canada. There is no reason why the same business transacted over the years in Canada by British and foreign companies should at the present time attract less tax at the present high wartime rates than the same volume of the same kind of business transacted over the same period of years by Canadian companies.

"Such adjustments in the present tax structure applicable to fire and casualty insurance would no doubt yield additional funds to the treasury and would distribute the burden of the tax fairly amongst all insurers, stock and mutual. The stock companies being profit-seeking organizations would pay a profits tax and the mutuals

would bear their share of taxation through a uniform premium tax. The cash mutuals would favour such a readjustment even if the premium tax made uniformly applicable to all insurers had to be raised above the rate the cash mutuals now pay."

We are not recommending that, but we are stating our position. It is this. We are not seeking to avoid paying our fair share of tax. Whatever this insurance industry should equitably pay, we want to bear our share; but not as a profits tax.

Now I come to our submissions:

"The cash mutuals therefore submit that the commission should find and recommend:

(a) That the premium tax under the Special War Revenue Act is inequitable and that it is in the public interest to amend that act so as to impose a premium tax at the same rate upon all fire, casualty and marine premiums paid either within or without Canada on Canadian business, whether written by stock companies (be the same domestic, British or foreign) or written by mutuals (domestic or foreign and however operating, whether on cash or premium note basis and including farm mutuals) or by reciprocals, to the end that all premiums paid by the public in Canada will reflect the incidence of the same tax.

"(b) That the income and excess profits tax acts as now enacted and administered are unfair to Canadian stock companies and that such acts should be amended so that Canadian companies will not be penalized because of being Canadian companies while British and foreign companies escape liability for tax upon income derived from profits on Canadian business and heretofore withdrawn

to foreign head offices so that Canadian companies pay on large amounts of investment income and British and foreign companies pay little or nothing on investment income.

"(c) That it is not in the public interest to apply or attempt to apply the income tax and excess profits tax acts to cash mutual companies because

"(i) The mutuals being non-profit organizations do not fall within the principles upon which the said acts are based which could only be applied to cash mutuals by an artificial and unwarranted definition of profits.

"(ii) Additional tax burdens should not be imposed on the cash mutuals as they perform valuable public services, namely:

"they provide fire and other insurance with complete security to a large part of the farming community and unprotected areas such as small towns, villages and other small rural communities which are not served by fire protection;

"they are independent and are not members of or under the control of the Canadian Underwriters Association which controls the business of and fixes rates for its members and as independents the cash mutuals tend to prevent unwarranted increases in the cost of fire and casualty insurance to the public.

"(iii) The incidence of Excess profits tax on the business of stock companies cannot be shown to have affected the volume of the stock companies' business or to have created a competitive situation so far as the stock companies are concerned; its only effect has been to drain off the stockholders'

excess wartime profits. These profits do not reflect themselves in increased cost of insurance to the public.

"(iv) While income and excess profits tax do not reach the mutuals this does not make their competition unfair.

"(v) The imposition of profits taxes on the mutuals would not contribute any substantial amount to the public treasury which could be augmented much more generously by amendments to bring under tax liability the investment income of British and foreign companies which now escapes although these companies enjoy the larger portion of Canadian business.

"(vi) The imposition of income and excess profits taxes on the cash mutuals could only result in more severe competition to the stock companies."

This is respectfully submitted, gentlemen, and I have here Mr. McIntosh and Mr. Foot whom I propose to call.

1. Introduction

The purpose of this study is to investigate the effects of the proposed system on the performance of the system. The study is divided into two main parts: a theoretical analysis and an experimental evaluation.

The theoretical analysis is based on the principles of the system and the results of previous studies. It shows that the proposed system can improve the performance of the system in terms of speed and accuracy.

The experimental evaluation is based on the results of a series of experiments. The experiments were designed to test the performance of the system under different conditions. The results show that the proposed system can improve the performance of the system in terms of speed and accuracy. The improvement is more significant when the system is used in a complex environment.

The results of the experiments are summarized in the following table. The table shows the performance of the system under different conditions. The results show that the proposed system can improve the performance of the system in terms of speed and accuracy.

The results of the experiments are summarized in the following table. The table shows the performance of the system under different conditions. The results show that the proposed system can improve the performance of the system in terms of speed and accuracy.

Submission of

The Gore District Mutual Fire Insurance Company,

The Economical Mutual Fire Insurance Company,

The Waterloo Mutual Fire Insurance Company,

The Perth Mutual Fire Insurance Company.

The Companies

The above-named companies are known as the Four Ontario Cash-Mutuals and each has carried on business for over seventy years. They are amongst the oldest of operating fire insurance companies, stock or mutual.

The "Gore District" was incorporated in 1839 under the provisions of Chapter 18 of the Statutes of Upper Canada, 6 William IV (1836) and has operated continuously for one hundred and five years. It was reincorporated by Dominion Special Act in 1937 - 1 George VI, cap. 48.

The "Economical" was incorporated in 1871 under the provisions of Chapter 52 of the Consolidated Statutes of Upper Canada 1859 and reincorporated by Dominion Special Act in 1938 - 1 Edward VIII, cap. 54.

The "Perth Mutual" and "Waterloo Mutual" were both incorporated in 1863 under the provisions of Chapter 52 of the Consolidated Statutes of Upper Canada, 1859, and have continued as originally so incorporated.

It is interesting to note the recital in the statute under which the Gore District was incorporated (6 William IV, cap. 18, 1836, carried over into the Consolidation of 1859 as cap. 52) which sets forth that "Divers loyal subjects have by their petition represented the great advantages that would arise from the introduction into this province of the principle of mutual insurance against losses by fire and prayed the interference of the Legislature to enable them to bring the said principle into effective operation." It is submitted that

great advantages did and continue to accrue from mutual insurance as will hereafter appear.

These companies originally carried on the fire insurance business only and while the bulk of their business continues to be fire insurance two of the companies write automobile and casualty lines. The large proportion of their business is in Ontario but some of them also transact business in Quebec and the western provinces.

Manner of Operation

The Four Cash Mutuals commenced as "premium-note" mutuals, insuring farm, village and local risks in south-western Ontario in the same manner as the many farm mutuals which have served the farming community in the absence (until recently and now only to a limited extent) of any general farm fire insurance service from the stock companies. It is estimated that over \$500,000,000 in farm fire insurance in Ontario (which is over 80 per cent of the total) is carried in mutual companies and that over 197,000 Ontario farmers are insured in mutuals (see Submission of Mutual Fire Underwriters' Association to Royal Commission on Dominion-Provincial Relations, 1938, copy attached).

The Four Cash-Mutuals insure at least 16,000 farm risks as well as a large number of village, town and other risks which are not protected by municipal or other fire-fighting organizations. Many of the stock companies will not insure these unprotected risks and in cases where farm risks are accepted the rates are higher than those available from the mutuals.

The Cash-Mutuals operate on a cash premium system as well as on the premium note basis. This development of the cash premium was a departure from the original scheme which relied on the premium note for the large part of the policy-holder's

premium. The mutuals always demanded some payment in advance as was required under the terms of the earliest legislation (6 William IV, cap. 18, 1836) and has been required by all legislation since.

As early as 1868 the Legislature recognized the need of permitting business on a cash mutual basis and authorized assessments for the purpose of establishing reserves.

The broad shift from reliance on premium notes, payable in arrears, to cash premiums paid in advance was brought about by the stock companies. In entering the fire insurance field the stock companies approached the public with the cry that the mutual policy holder's liability was never fixed but was undetermined and unlimited, and that a mutual policy gave no security.

It was this kind of competition that forced the more enterprising of the Canadian mutuals into the cash premium method of doing business and forced them to set up such reserves as would make quite manifest that the mutuals were just as safe to insure with as the stock companies.

The stock companies having been deprived of these sales arguments, fallacious as they were (because we know of no Canadian mutual that has defaulted) now come forward with a plea that they are subject to unfair competition taxwise, which is contrary to the facts as will hereafter appear.

The shift from the premium note method to the cash premium method did not alter the mutual and non-profit nature of the business of the mutuals.

The mutuals came into being from necessity as a banding together of property owners whereby fire losses suffered by the few would be borne by the many and thereby the individual at small cost was saved from the loss that otherwise would be calamitous. Mutuals and stock companies as well con-

Mr. Robertson

tinue to serve this purpose with this difference: A mutual company is the creature of and is owned by its policyholders only; it functions to protect its policyholders against loss and operates entirely without profit. A stock company on the other hand is the creature of and is owned by its stockholders and for a consideration and prospective profit to its treasury and its stockholders offers to protect its policyholders against loss. The objects of the two classes of companies are basically different. A mutual company seeks to give protection and reduce rates as nearly to cost as possible.

"To provide security the mutuals as their business has increased have built up reserves against conflagration and contingency and at the same time have constantly reduced their rates as conditions warranted. On the other hand stock companies while seeking to set up adequate reserves strive to make profits for their shareholders. That stock companies have been successful in their endeavours to make profit is established from p. xviii, Vol. 1 of the 1942 Report of the Superintendent of Insurance where it appears that since 1875 down to 1942 (inclusive) Canadian stock companies had paid dividends to their shareholders of \$42,395,000 and in the year 1942 alone the stock companies paid \$1,479,000 in which year they enjoyed only 36 per cent of the premium income."

Stockholders of British and Foreign companies as well no doubt enjoyed handsome dividends derived from Canadian business.

This submission is not critical of the profit motive of the stock companies nor of the handsome dividends they have paid but cites this very large dividend disbursement to emphasize the essential difference between the mutuals and the stock companies and the fact that in spite of being taxed on income the stock companies have not seriously suffered.

Mr. Robertson

The stock companies complain of tax discrimination, in that they are called on to pay income and excess profit tax while the mutuals are not. It cannot be too strongly emphasized that these taxes are profit taxes and as such have no application to the operation of mutuals but must be applied to the operations of the stock companies whose underlying purpose is the making of profit. That they have made large profits over the years is manifest from the figures of dividend disbursement above set forth.

In the case of the stock companies there is a conflict between the interest of the stockholder and that of the policyholder. With the stock companies it is desirable to maintain as high rates as competition will permit and to select only the choicest risks so that dividends will be as great as possible. In contrast, in the case of mutuals there is no such conflict. The whole reason of their existence is protection and in consequence there is no motive to maintain higher premium rates than necessary to provide that protection from day to day, with adequate reserves to meet contingent unusual underwriting losses.

It is an accepted fact that the mutuals' rates have been consistently lower than those of the stock companies. It is a reasonable inference that with profit the main motive of the stock companies, the rates would not have come down as they have done in recent years except for the mutual competition. Now that the mutuals have met the criticism of "uncertain liability" by going on the cash premium basis and the criticism of "insecurity" by a record over many years without a single default and by establishing adequate reserves against unexpected losses the stock companies are now attempting to ease mutual competition by securing the imposition of a profit tax on a non-profit operation.

Profit Taxes Have No Application to Mutual Operation

The mutuals at the time of preparation of this submission are not aware of the position the stock companies will take other than press reports of complaints of unfair tax burdens on stock companies which deal with the public in the same manner as mutuals and the suggestion is made that the mutuals should therefore be taxed. There is no disclosure of how the mutuals should be taxed or what moneys of the mutuals will be said to be "profits".

It is submitted that to impose income or excess profits tax on mutuals would be a complete departure from the principle of these statutes which are "profit" taxing statutes and the mutuals are non-profit organizations of policyholders.

With mutuals the excess of premium income over losses plus expenses is returned to policyholders (not stockholders) as premium rebates (sometimes called policyholders' dividends) or is held for the policyholders in reserve to protect against future unusual losses. These premium rebates have no element of profit in them as is aptly put in the following quotation taken from 1905 Report of the Income Tax Committee in England, the quotation being taken from

"The Fundamental Principles of Taxation" by Sir Josiah Stamp:

"The suggestions made to us that the 'dividend' which is paid to members of these societies constitutes a profit which would properly be taxable, rest, we think, on a misapprehension of the nature of the dividend. The so-called 'dividend' arises from the fact that the prices charged by the society to its members are in excess of cost price. If the goods were distributed at the exact price, there would be no 'dividend', and it follows that no question of income tax could arise.

But the societies, for what they consider good reasons, prefer to fix a scale of prices which leaves a margin over the above cost. Thus an adjustment has to be made periodically, and the balance between cost price and distributing price is divided among the members in proportion to the value of their purchases. This 'dividend' is clearly not profit, but merely a return to members of sums which they have paid for their own goods in excess of the cost price. There can be no doubt that the procedure which we have described - resulting as it does in periodical returns to members - is conducive to thrift, and we see no reason for discouraging it.

"A Society may, however, of course, make profit on dealings with non-members. This profit, is in the case of most ordinary societies, very small in amount. But, so far as any such profit is made, and so far as any interest is paid on capital, if that profit or interest comes into the hands of any person whose income is over £160, it ought to be, and it is taxable."

While the above quotation refers to trading cooperatives it is equally applicable to premium rebates to mutual policy holders. There is this difference that with mutual insurance it is security that is furnished not goods or merchandise and there is no element of profit involved in any single transaction or the overall operations of the Company.

"Underwriting Profit" (and Loss), a term widely used in insurance literature, means only the excess of premium income over losses and expenses. As applied to a cash mutual company it means only that its amount is available to reduce future premiums or meet future losses. In contrast with a stock company the term "underwriting profit" means that

the management has added a profit to the stockholders' account from which in the current or future years dividends can be paid to stockholders. In the case of stock companies it has no relationship whatever to present or future cost of insurance; if not immediately disbursed as dividends it may go to reserve, there to be the property of the shareholders, not the policyholders, and while it may contribute to the security of policyholders it is a protection to the stockholder's invested capital and is a profit thereon and as such is and should be taxable.

The above distinction is well recognized in income tax law. The principle has been stated to be that income tax charges what goes into the taxpayer's pocket and not on what his pocket is saved. See *Tennant v. Smith* (1892) A.C. 150.

In the case of the mutuals the "Underwriting Profit" saves the pocket of the mutual policyholder something on his current or future insurance cost whereas in the case of stock companies the underwriting profit goes into the pocket of the stockholder. Reference is here again made to the enormous sum of over \$42,000,000, paid in dividends by Canadian stock companies since 1875 as above mentioned.

The stock companies will no doubt, in their representations to the Commission, refer to the income derived from the large reserves of the cash mutuals and, purporting to speak on behalf of the common weal in wartime, complain that this income escapes tax while in the hands of the stock company is liable to tax.

An answer to this is found in the table on page xiv of the Dominion Superintendent's Report for 1942 from which it will be observed that the dividends paid to shareholders by the stock companies listed are, in total for all companies, approximately one-half of the total of the companies' invest-

ment incomes. The total of investment income is \$3,358,928, and the dividends \$1,691,700. In the case of the mutuals the investment income goes to reduce premiums or for further security goes into reserve - it has no element of profit.

Indeed an analogous situation exists in respect of life insurance companies. They possess large investments from which they derive income. The investment income is an essential element in the determination of their rates. As the interest rate goes down the cost of insurance goes up, as has happened recently because of the current trend of interest rates to lower levels. Admittedly the principles of life underwriting are, of their very nature, on a more scientific basis than those of fire or casualty insurance but in every calculation interest is an element in the determination of fire and casualty rates.

It is significant that the stock life insurance companies have made no complaint against taxation on that part of the companies' investment income credited to shareholders account nor have they complained that because their profits credited to shareholders account are taxed they are suffering unfair competition from the mutual life insurance companies. It would appear that while disliking high wartime profit taxes the life insurance business recognizes the presence of profit, which they seek, in the operation of a stock company and its absence in the operations of a mutual company.

The cash mutuals accumulated the bulk of their reserves while operating under provincial registry. The Ontario statutes recognized the need of security as it evidenced by Section 275 of the Ontario Companies Act, R.S.O. 1937, cap. 251 which reads as follows:

"(1) Subject to the provisions of subsection 5, a mutual or a cash-mutual insurance corporation may form a permanent

reserve fund, to consist of such part of the net profits as may from time to time be set aside by the directors for that purpose; or to be made up by annual assessments for that purpose not exceeding, for any single assessment, ten per cent on the premium notes held by the corporation, until the total fund reaches two per centum of the corporation insurance in force.

(2) Such funds shall be held for the security of the insured and shall be subject to the provision of this act relating to the investment of the funds of insurance companies.

(3) The net income from the fund shall be included in the general receipts of the company, and shall constitute a part of the "net profits", if any, as defined in this section.

(4) The fund so accumulated shall be used for the payment of losses and expenses when the cash funds of the company in excess of an amount equal to its liabilities (including guarantee capital, if any) are exhausted, and when the said fund is drawn upon the allocation of profits or assessments as aforesaid may be retained or continued until reached.

(5) The said fund may not be reduced by the payment of dividends to shareholders or members, or by a reduction of current premiums below the limit of two per cent of the insurance in force hereinbefore mentioned, but it may be increased beyond the said limit if the company so desires.

The above statutory provision clearly indicates why the Ontario cash mutuals which over the years have accumulated large reserve funds are in such a strong financial position to-day.

The following table shows the net amount of fire insurance under the policies of the cash mutuals at the end of December, 1944, and the amount of their respective surpluses:

	<u>Net Insurance in Force</u>	<u>Surplus</u>
Gore District	\$123,415,863	\$2,508,573
Economical Mutual	114,057,549	2,940,246
Waterloo Mutual	83,690,151	1,988,356
Perth Mutual	46,982,771	1,818,304

It is to be noted that all of the companies hold reserve funds not greatly in excess of two per cent of the insurance in force. The proportion of the total reserves held for casualty insurance is in no case unreasonable in amount.

The Mutuals' Method of Operation in contrast to that of the Stock Companies tends to lower insurance costs and is therefore in the public interest

It is submitted that it is not in the public interest to impose income or excess profit taxes on the mutuals. They have served the insuring public in Canada efficiently from very early times and have survived as an effective agency against the monopolistic tendencies of the stock companies, exercised through Canadian Underwriters' Association and towards keeping insurance costs down. (See pages 61 and 62 of the Masten report on insurance, copies attached, Appendix pages 27 and 28.)

The cash mutuals on whose behalf this brief is submitted were all in business prior to the formation of the Canadian Underwriters' Association (originally the Canadian Fire Underwriters' Association). This association, originally formed in 1883, is associated with similar organizations in western Canada and the Maritimes and all are subject to the overall direction of the Dominion Board of Insurance Underwriters. These associations are not public bodies or organizations.

They are creatures of the stock companies and exercise control over their members in respect to rates, commissions, maps, plans and forms of contracts. While we have no certain knowledge of the facts it is believed that all or almost all of the companies constituting the membership of the association are British and foreign companies or controlled by British and foreign companies. It is suggested that the association be requested by the Commission to disclose this information.

Under the rules of the Association a member must not reinsure with or accept reinsurance from a non-member. Its membership includes approximately 160 stock companies (there were 263 companies registered under the Dominion Act in 1942) so that it is obvious that a large part of the reinsurance facilities which in a free market, and on merit, should be open, are closed to the independent companies. The Association will not admit a mutual to membership. Indeed, in the early days the Waterloo Mutual was a member but some years ago was forced out.

The Canadian Underwriters' Association has since the imposition of the necessary high wartime taxation inaugurated a business promoting scheme called its agency registration plan, a copy of which with relevant material is attached hereto. (Appendix pp. 29-43). While the agency registration plan may or may not be a transgression of the wartime salaries control regulations it is certainly not calculated to lessen the cost of insurance of the insuring public. Under this plan an agent received an extra five per cent commission if seventy-five per cent of his business goes to board companies; if less than fifty per cent of his business goes to board companies the Association withdraws its facilities (rating manuals, plans, etc.). This scheme can have no other effect than increasing insurance costs as it leads to switching

of risks with the attendant expense of such a practice. It also drains off from taxable profits an additional five per cent by way of commission and in this connection it is to be observed that this additional five per cent is not on new business but on all business if the agent gives seventy-five per cent of his total business to the stock companies, members of the Association.

Mr. Hartley McNairn, K.C., then superintendent for the province of Ontario, commented on the agency registration plan, then and since being pressed by the Canadian Underwriters' Association, as follows:

"The main principle involved in the above plan of remuneration is to pay the agent in relation to the volume of business placed with tariff companies. It is a competitive basis designed to attract business from competitors through the incentive of an increased commission rate. It ignores the sound principle of payment to the agent in relation to services rendered.

"This plan may lead to increased competition in the commissions paid to agents and, if so, will result in a further increase in the cost of doing business which is already at a high level. Fair competition in insurance rates is a healthy condition tending to produce a reasonable cost to the insured. Competition in commissions can only retard or prevent reduction in rates and increase the cost to the public."

(See pages x and xi of the Ontario Insurance Superintendent's report on the year 1941, published 1942).

This is the kind of competition the mutuals have to meet from the stock companies who now come forward complaining that mutuals which are non-profit organizations should be made subject to a "profit" tax.

Another factor which contributes largely to the cost to the public of insurance written by the stock companies is the practice of operating through the so-called "pup" companies or "fleet operation." No doubt the stock companies are finding that their many controlled or subsidiary companies (fleets) are an expensive luxury under the Excess Profits Tax Acts. The "pups" are no doubt good business getters but as each is subject to separate tax they may now be found to be embarrassing.

That the Dominion Superintendent of Insurance was concerned as to the effect of fleet operation on the cost of insurance to the public is evident from the statements on p. lxviii of the Dominion Insurance Report for 1940. Here attention was drawn to the disproportion between the increase in aggregate fire and casualty insurance premiums and the number of licensed companies in the field and to the development of fleet practice as the probable explanation.

On May 6, 1941 the superintendent directed a letter to the various companies on the subject of fleet operation from which we quote as follows:

"While the accuracy of this analysis on the expense problem has not been contested it is evident that no action has been taken by those responsible for the fleets themselves to reduce the number of companies operating under their supervision and as all deplore the gradual increase in the expense of operation it must be assumed that there are good reasons for the continuance of fleet practice or serious obstacles in the way of its discontinuance. The purpose of this letter is to ask you as representing one of the groups mentioned for an expression of opinion on the following points: 1. Would the elimination of the subsidiary or any of the affiliated companies of your

group or groups reduce the premium income of your office? If so, could that result be avoided by changes in existing restrictions on agency representation? 2. Would the expense ratio of continuing companies be reduced as a result of such elimination? 3. Has any consideration been given to such elimination and, if so, what are the objections thereto?"

No person outside the superintendent's office so far as is known, has any knowledge of whether any replies were received and if received, what were the answers to the questions propounded.

Examples of fleet operation are evident from the lists on pp. 36 to 45 (inc.) of Canadian Fire Insurance Year Book 1944 published by Stone & Cox Limited. Copies of these pages are attached to this submission (Appendix p.44). The commercial union group of eleven companies as shown on p. 37 is an example. Here we have eleven companies under one direction but each of the eleven might have a separate agent in each community which undoubtedly increased the cost of insurance to the public.

The purpose of fleet operation is of course well known. The number of agents any one company can appoint is definitely limited and the limitations of agencies limits premium income. This limitation is overcome by fleet operation under the control of an admiral, the general manager of the parent company which is often a foreign corporation. Where this fleet control lies can be learned from an examination of the 1942 report at p. 918 where lists of directors are given, and also the groupings listed in the pages of the Stone & Cox year book attached.

The cash mutuals from their very nature cannot and do not operate fleets but must meet fleet competition, but the

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fleet operators would have us believe that they suffer unfair competition by having to pay taxes on their profits and wish in some manner to have additional taxes imposed on the non-profit competition of the mutuals.

In connection with the advantage to the public of having competition from other than board companies, the attention of the Board is directed to pp. 31, 32 and 33 of the Masten report (copies of which are attached, Appendix pp. 45, 46 and 47). It appears from this portion of the report that shortly before the late Mr. Justice Masten was appointed to investigate and report on Ontario insurance laws, that the tariff companies (stock companies members of C.U.A.) had, in manner similar to that now being adopted, approached the Minister of Finance with the request that their competitors, the unlicensed insurers, be subjected to a special tax. The General Manager of the Canadian Manufacturers Association then gave evidence on behalf of the Canadian Manufacturers Association opposing the tax then proposed. A copy of a portion of this evidence as quoted by the Honourable Mr. Justice Masten makes interesting reading and is relevant to the situation now before this Commission.

Present Rates under Special War Revenue
Tax Act Discriminate Against Mutuals.

The taxation on fire and casualty companies falls under three statutes, namely, Special War Revenue Act which taxes premium income and the Income and Excess Profits Tax Acts which tax profits.

The rates under the Special War Revenue Act, 6 George VI cap. 32, sec. 14, are as follows:

<u>Stock Companies</u>	<u>Cash Mutuals & Lloyds</u>	<u>Cash Deposit Mutuals & Reciprocals</u>	<u>Marine</u>
2 per cent	3 per cent	4 per cent	nil

The tax is imposed on "net premiums" as defined in the Act. In the case of companies operating on the deposit premium plan and reciprocals, the interest earned at the average rate on the amount by which the premium deposit exceeds the net cost, is added to the amount of net premiums. In the case of the deposit premium mutuals the unabsorbed premium deposit is deducted from the gross premium deposit in ascertaining the net premiums to which the tax is applied.

It will be noted that there is no uniformity under this Act in the taxation of the companies operating in the insurance field. The stock companies have raised a great outcry that they are discriminated against under the Income Tax and Excess Profits Tax Acts but we do not hear them or any of their agency organizations in the press or by submission to this Commission drawing attention to the preference they receive under the Special War Revenue Act.

It will be observed that the stock companies' tax under this Act is one-third less than the tax on cash mutuals and only half the tax on other mutuals and reciprocals while the marine business which is wholly in the hands of the stock companies escapes entirely.

Marine Exemption

The marine premiums on business in Canada in 1942 (p.c.c. of 1942 report) was as follows:

Canadian companies	\$ 563,493
British companies	6,680,367
Foreign companies	<u>7,050,716</u>
	\$14,294,576

So we have \$14,294,576 stock company marine premium income which totally escapes the premium tax. Of this the large portion goes into the coffers of non-Canadian companies.

The figures as to assets in Canada for marine protection are even more startling. For example, the Eagle Star

collected in 1942 (p. c.c. of 1942 report), \$1,131,314 in premiums against which it held assets of \$17,543 only and the Sun Assurance enjoyed a premium income of \$1,033,270, but had no assets in Canada in respect of marine business. It is also observed that no company doing marine business in Canada received in Canada any income other than premium income except the Hartford which reported \$2,121 other income. Taking the totals for British and foreign countries only we have total premium income in Canada for marine business of \$13,731,083, total losses in Canada and other expenses in Canada of \$9,514,753 (\$7,576,384 plus \$1,938,369) which deducted from the total premium leaves \$4,216,330 excess, as a net premium income apparently siphoned out of Canada which bears no premium tax, Income or Excess Profits Tax. Furthermore, most of these non-Canadian companies writing marine insurance and enjoying this preference as to premium tax also write fire and in many cases casualty insurance directly and through Canadian subsidiaries. Besides the marine premium tax preference they also enjoy special advantages in the way of escaping income and excess profits tax on investment income under the fiction that such investment income is earned at a head office outside of Canada as will hereinafter be discussed.

This premium tax preference has paid the stock companies handsomely and it is to be observed (pp. cc. & C.C. i of 1942 report) that the premium income for marine business of the British and foreign companies jumped over 100 per cent in 1942 over 1941, no doubt as a result of increased marine traffic, but the stock companies do not wish to pay excess profits tax or income tax on the resulting increased profits enjoyed during wartime and directly attributable to the war.

Unfair Preference in Favour of the Stock

Companies Under the Special War Revenue Act

Referring to the table of distribution of fire insurance in Canada on p. lxi of the 1942 report it appears that 20.95 per cent of the total fire premium income went to purely Canadian companies, 40.14 per cent to British or British controlled companies and 38.91 per cent to foreign controlled companies. From tables on pp. cxiv, cxvi and cxx we observe the total net premium income on fire and casualty insurance in Canada in 1942 was as follows:

Total Net Premiums

	<u>Fire</u>	<u>Other than Fire</u>	<u>Total</u>
Canadian companies	15,699,206	20,607,559	36,306,765
Deduct mutuals - Clare, Economical, Gore District, Kings, Picton, Wawanesa, Portage la Prairie	<u>2,973,134</u>	<u>1,465,669</u>	<u>4,438,803</u>
Canadian stock companies	12,726,072	19,141,890	31,867,962
British stock companies (p.cxviii)	16,394,992	12,641,096	29,036,088
Foreign (including foreign mutuals) (p.cxxiv)	<u>19,140,329</u>	<u>6,629,862</u>	<u>25,770,391</u>
Total Premium Income to Canadian stock & British and foreign companies			86,674,441
Premium Income of other mutuals		3,553,463	
Premium Income of reciprocals		<u>936,571</u>	<u>4,490,034</u>
Stock companies' Premium Income (Canadian, British & Foreign)			82,184,407

so that we have

Premium income to <u>stock companies</u> paying 2% on	\$82,184,407
Premium income to <u>Canadian mutuals</u> paying 3% on	4,096,525
Premium income to <u>other mutuals</u> paying 4% on	3,553,463
Premium income to <u>reciprocals</u> paying 4% on	936,571

In the result the stock companies are receiving a preference of 1 per cent as against cash mutuals on over \$82,000,000 of premium income and a preference of 2 per cent as against other mutuals and reciprocals.

A preference of 2 per cent on \$82,184,407 is equivalent to a tax saving of \$1,643,688 to the stock companies over foreign mutuals and reciprocals and a preference of 1 per cent over cash mutuals is a saving of \$821,844.

Now let us examine Table A on p. lxvii of the 1942 report. We see here that the total income tax paid by stock companies amounted to \$1,619,458, a figure not materially different from the preference in rate that they saved as against their competitors under the Special War Revenue Act.

Admittedly they pay \$2,733,455 under the Excess Profits Tax Act. But why should they not be liable to excess profits tax? They are in business to make profit (as contrasted with the mutuals) and should not be treated differently from any other profit-seeking organization under the tax laws.

The Canadian stock companies have not suffered as is evident from the totals on p. xcix of the 1942 report where it appears that the total assets in 1941 were \$99,285,379 and had increased in 1942 to \$104,438,721 in spite of wartime taxes to which the stock companies were subject. The totals for Canadian companies on p. cvii of the report confirm this because they show that while the capital stock had decreased some \$96,000 the excess of assets over liabilities (excluding capital stock) had increased by \$2,083,365 (\$61,468,974 less \$59,385,609).

In the end result so far as Canadian stock companies are concerned while they paid \$1,657,822 in income and excess profits tax in 1942 to help the war effort they were able to pay back capital of \$90,000 and to increase their assets in Canada by \$2,083,365.

This view is further supported by the totals on p. xv of the report where we see that the net gain for Canadian companies was substantial, viz., \$1,965,022.

British and Foreign Stock Companies Enjoy
A Further Peculiar Tax Preference by Avoid-
ance of Tax on Investment Income.

If we refer to the 1942 report beginning at page lxviii we find the average rate of taxes on the underwriting profits to be as follows:

1940:	Canadian companies	-	66.9
	British companies	-	29.0
	Foreign companies	-	25.3
1941:	Canadian companies	-	67.3
	British companies	-	31.2
	Foreign companies	-	34.6
1942:	Canadian companies	-	73.3
	British companies	-	51.5
	Foreign companies	-	48.2

In so far as Canadian stock companies are concerned the taxes imposed under the Income Tax Act and the Excess Profits Tax Act do not bear any relationship to the underwriting profits alone. In the case of Canadian companies these taxes are imposed on the underwriting profits plus all income from invested assets and, as the income from the latter source is considerably greater than the underwriting profits from the insurance account, the taxation of Canadian companies is considerably in excess of the taxation of British and foreign taxable income. No British or foreign company had all its underwriting profits taxed away. (p. lxxiv and p. lxxv) Canadian stock companies, however, writing \$11,521,235 of business had underwriting profits of \$383,172. (p. lxxiii) The taxes paid amounted to \$547,993. (p. lxxiii)

These Canadian stock companies are, in some respects, similar to the four cash mutuals who have retained the greater part of their earnings for the security of their members as required by law for cash mutual companies.

If by way of example we refer to the 1942 report, page 558, we find that the Phoenix fire had an underwriting loss of \$9,433.96. The interest earned was \$15,388.37 and the

total net gain about \$6,000.00; result - no taxation other than premium tax. Looking at page 350 we see the Hartford fire had an underwriting loss \$6,148.58, interest earned \$40,442.35; result - no taxation. The Yorkshire (p. 784) appears to top them all - underwriting gain \$1,339.50, investment income \$130,727.98, total income and excess profit taxes \$266.80. These are three cases taken at random.

Had these companies been Canadian stock companies with their assets in this country the Income and Excess Profit Tax Acts would have made them subject to at least forty per cent of the net gain which would have included the income on investments held in reserve for the protection of policyholders. However, their income although it is earned on moneys paid by Canadians is notionally received at the companies' head offices outside Canada and so escapes income and excess profits taxes.

The interest earnings of most of the foreign and British companies, as shown in the superintendent's report, bears no relationship to the interest on the value of bonds and debentures on deposit with the Receiver General. The following are examples. the Commercial Union, page 191, 1942 report, held on deposit with the Receiver General - \$932,594.20, interest earned - \$2,772.00; the Helvetia Swiss, page 353, held on deposit with the Receiver General - \$167,608.00, interest earned \$750.00; the Royal Exchange, page 647, held on deposit with the Receiver General - \$864,656.00, interest earned - nil; Pearl Assurance, page 582, held on deposit with the Receiver General \$803,584.00, interest earned \$6,721.50

Looking at the tables on pp. cxiv to cxxv of the 1942 report we find the income in Canada of the different classes of company, taking the totals of the column headed "Income, rents and dividends on stocks earned" -

Canadian companies	British companies	Foreign companies
\$3,408,274	\$860,786	\$1,097,553

but as appears from p. lxii (Table B) and p. xx (2nd Table) of the 1942 report the several classes of companies enjoyed the Canadian business in 1942 in the following proportions:

Canadian (including British & foreign controlled Fire Casualty	British	Foreign
12,636,228 (26.23%)	16,394,902 (34.03%)	19,140,329 (39.74%)
17,163,984 (34.1%)	12,642,254 (25.2%)	20,328,965 (40.7%)
29,790,212 (30.3%)	29,036,156 (29.3%)	39,469,294 (40.4%)

It is to be observed that Canadian companies enjoying only 30.3 per cent of the total business have all their investment income \$3,408,274 included in profits for tax purposes while British and foreign companies enjoying 69.7 per cent of the total business earn only \$1,958,339 investment income in Canada and this is not included in profits for tax purposes.

We submit the above clearly establishes the inequitable incidence of income and excess profits taxes whereby the Canadian stock companies are caught and bear the burden of taxation and British and foreign companies enjoying over two-thirds the business escape. In no case, except in the case of Canadian incorporated companies, does the interest from investments form a part of the taxable income.

It will be observed that the inequitable incidence of income and excess profits tax arises from the difference between the manner of computing "income" to which to apply tax against Canadian stock companies and the manner of computing the "income" of British and foreign companies and this inequity should be remedied.

What happens is that "income" of Canadian companies includes the income received from the investment of its capital reserves and unearned premium as well as its so-called

"under-writing" profit. In contrast in the case of British and foreign companies very little (if any) investment income is so included as taxable income on the theory or fiction that the investment income of a company having its head office out of Canada is received at the head office out of Canada and as it is supposed to pay the head office expenses referable to Canadian business it is not to be included in the income of the company for the purpose of income and excess profits taxes.

Only the "underwriting profit" of the British and foreign companies is taxable. Investment income escapes tax to the prejudice of the treasury and the purely Canadian company.

It appears therefore that an examination of the statistics of the reports of the insurance department shows that Canadian stock companies have a just complaint as to the inequitable incidence of income and excess profits taxes but this complaint cannot be against the mutuals but should rather be directed against British and foreign companies. Possibly the complaint here referred to has not been made because of "fleet operation" and because of British and foreign control of Canadian companies. It may be that the fair treatment of the Canadian company is subrogated to the greater interest of the business in Canada of the British or foreign company.

The above statistics point to the one conclusion, namely that Canadian stock companies have retained in this country all their assets and have conserved these assets in order to offer a security equal, if not greater, than those of the British and foreign companies. In contrast, British and foreign companies have withdrawn the greater part, if not all, of their underwriting profits and also the interest received on deposits with the superintendent and on premium money collected in Canada.

The four cash mutuals and other mutual insurance companies, in order to combat the fierce propaganda which has been issued by stock companies for years, have found it absolutely necessary to conserve, to a greater degree than the stock companies, their distributable surplus.

The application of the Income Tax Act and the Excess Profit Tax Act bears little relationship in so far as Canadian companies are concerned to the underwriting profits and, as pointed out above, a number of Canadian stock companies have paid in the form of income tax and excess profit tax considerably more than the underwriting profits made by those companies. However, taking into consideration the most extreme stock company cases, it would not compare with the application of these acts to cash mutuals where in 1942 the four cash mutuals made an underwriting gain of \$77,531, their income from reserves was \$390,475, or a total of \$468,006. The minimum payable on this income based on forty per cent would have amounted to \$187,202 or approximately 250 per cent of the underwriting gains for that year.

In view of the fact that by far a greater proportion of Canadian insurance is written by British or foreign companies who have continuously removed their underwriting profits from this country and who do not appear, even to-day, to pay an income tax or excess profit tax on their interest from investments, we cannot subscribe to the theory that it would be equitable taxation to apply these acts to cash mutual insurance. Their income from investments is an integral part of their premium and forms a greater part of the security for the policies of the thousands of people whom they insure.

Competition

The stock companies complain of unfair competition tax-wise but an examination of the statistics in the Superinten-

dent's report for the year 1942 indicates that they have not been badly hurt. In addition to increasing their assets as above mentioned in this submission they still were able to pay dividends to stockholders of \$1,479,112 in 1942 as against \$1,714,835 in 1941, a decrease of only \$335,722 (see p. xviii). It appears that the stock companies' reduction in dividends disbursed did not differ greatly from the amount of increased taxes which merely reflected increased profits to shareholders' account. Their total income and excess profits taxes were \$1,362,920 in 1941 and \$1,657,822 in 1942, an increase of \$294,902, and total expenses after deducting income and excess profits taxes (as given in footnotes on p. xviii) increased by \$1,006,728. In noting the large increase in expenses which occurred in spite of Wartime Prices and Trade Board freezing of salaries, etc. one wonders if such increase would have taken place in the absence of excess profits legislation.

The stock companies suggest that the competition they complain of would be eased if these "profit" taxes were made to apply to mutuals.

Let us suppose they were so applied. Presumably the suggestion is that they should apply to the underwriting gain plus investment income of the mutuals. Such an application would constitute an additional annual expense and no doubt the stock companies hope that this additional expense would be reflected in increased premium rates which would lessen competition.

This, it is submitted, would not be the result, certainly not immediately, unless legislation were passed prohibiting mutuals from lowering rates because the mutuals desiring only to give protection have no incentive to make profit to which a profit tax could attach. The inevitable result where

adequate reserves are already set up would be to lower the mutuals' rates to the point where the underwriting loss (including expenses) would equal the investment income on reserves so that in the end no taxable profit would be shown and instead of relieving themselves from the competition of the mutuals the stock companies would, in the meantime at least have to meet still lower rates than those they now compete with. That the cash mutuals are not desirous of making an underwriting profit is evident from the table hereto attached of premiums written (less return premiums) and underwriting profits or losses for the years 1937 to 1944 inclusive. (See Appendix p. 48) From these tables it will be observed that the underwriting profits for the four cash mutuals for the years mentioned were only 1.24 per cent.

Or if the imposition of a profit tax did not result in the case of the cash mutuals in lower premium rates the same absence of profit motive would likely lead to an increase in the rates of commission to agents which are admittedly lower than those paid by the stock companies. This would likewise result in more competition which is just what the stock companies are complaining of.

It may be that the real purpose of the stock companies' attack on the mutuals is to prevent the mutuals from having moneys to add to their reserves as security for policyholders and thereby over the long term ultimately get rid of this class of independent which is not controlled by the rules, regulations and rates of the Canadian Underwriters' Association or permitted to join the association or reinsure with its members. The imposition of profit taxes on the cash mutuals would undoubtedly contribute over a long term in preventing their growth.

It is submitted that it is not in the public interest to

impose taxes which can possibly have the result of preventing the development of mutual insurance.

There is no suggestion that the mutuals have at any time grown rapidly and in particular there is no suggestion similar to that made in reference to the Western Co-Operatives that they have had an unusually rapid growth during the period of the application of high wartime taxes. The mutuals have not been expanding except in a normal way. They have not been buying out other businesses or going into other lines of business unrelated to their main operations. Their growth has been normal in the face of fierce competition from the stock companies and has taken place only because of efficient service to policyholders desiring security and protection at reasonable rates.

Mr. W.E. Baldwin, then president of "All Canada Insurance Federation," an organization of some two hundred licensed companies carrying on fire and casualty business throughout Canada, contributed three articles to the Journal of Commerce and Commercial, New York, in December 1939, December 1940 and December 1941. Dealing with the question of reduction of rates he said in the article in the issue of December 1939,

"In Ontario and Quebec, however, notwithstanding the fact that much time has been spent on attempting to present a revision of rates which would reflect the excellent experience on a number of classes, no action has been taken on the programme suggested. On one pretext or another every effort to bring about a change that would allow the public to benefit from the promulgation of lower rates, and at the same time permit the associated companies to meet non-tariff competition has been effectively blocked.

"Results of the last few years, in themselves present an open invitation to the governments of the two provinces to

step in and do for the public that which the companies seem either unable or unwilling to do."

In the article appearing in the issue of December 1940 it was pointed out that no changes had been made in commission rates to agents and he said,

"It is reasonable to anticipate that the end of 1940 will terminate an era of seven years in Canada during which the loss ratio has only twice been about 40 per cent and the average for the period is 37.78 per cent predicted on our estimates for 1940 being approximately correct.

"Owing to the inability or unwillingness on the part of tariff rating associations to face the situation, and bring fire rates down to a figure that will not produce an abnormal profit, the non-associated companies continue to augment the volume of income they are writing in the dominion. The results of their operations show clearly that they are able to make a handsome profit while putting liability on their books at substantially lower premiums than those quoted by companies who are members of the tariff associations."

And in the last article appearing in December 1941 the following appears,

"While some headway has been made by the territorial boards in Canada toward substantial rate reductions, the Canadian Underwriters Association has maintained its record of masterly inactivity in so far as Ontario is concerned. Outside of the reduction brought about by the writing of mercantile policies for three years, no general rate reductions have been made and many rates are entirely too high, as the continuing favourable loss ratio clearly indicates."

The above quotations indicate that although the stock companies were then subject to income tax (although not to excess profits tax) they took no steps to reduce the rates in

spite of their very favourable experience and appear to have maintained their "record of masterly inactivity" so far as the public is concerned.

Here is the chief executive of a body largely representing stock companies whose statements do not indicate that income taxation of their profits was creating any serious competition.

Conclusion

The Ontario cash mutuals have no wish to avoid bearing their fair and equitable share of national taxes.

However, the cash mutuals submit that regardless of legalistic arguments based on English tax legislation which differs materially from existing Canadian tax legislation or based on English decisions interpreting English legislation, a profits tax of its very nature has no application to their activities. It is further submitted that before any attempt is made to apply profit taxes to mutual insurance operations the apparent glaring inequities in the present tax structure applicable to insurance should be remedied.

It is the view of the cash mutuals that the premium tax under the Special War Revenue Act should first be adjusted so that all insurers, mutual and stock, would be charged the same rate on net premiums, whatever such rate might be, and that the preference whereby marine premium money paid by Canadians now escapes premium tax and the preference in favour of stock companies whereby they pay 1 per cent less premium tax than any other class of insured, should also be removed. The remedy of these inequities would be in the public interest because this type of tax would bear evenly on the whole fire and casualty business and would reflect itself to the same extent in all premium rates charged the insuring public. If these views are adopted the public inter-

est would no doubt be served in the way of increased income to the treasury.

It is the opinion of the cash mutuals that the preference now enjoyed by British and foreign stock companies whereby the bulk of their investment income escapes liability for tax, should be eliminated. It is suggested that the remedy could be provided by legislation which would include in the taxable profits of British and foreign stock companies an item for investment income. It is suggested that the remedy could be provided by legislation which would lay down a rule for the determination of the amount of investment income of British and foreign companies that would be brought into account for taxation purposes and such legislation in order to do equity should apply the same rule in respect of the amount of the investment income of Canadian companies made liable to tax. Such a provision would make for equality of treatment and the Canadian companies would not be penalized in the way of having all their income from investments accumulated over the years made liable to tax as contrasted with the situation obtaining in respect to British and foreign countries who over the years have earned profits in Canada on Canadian business and have withdrawn these profits and the investments representing these profits out of Canada to their home offices so that under the present tax framework the income on past years' profits to-day escape tax because they are not in Canada. There is no reason why the same business transacted over the years in Canada by British and foreign companies should at the present time attract less tax at the present high wartime rates than the same volume of the same kind of business transacted over the same period of years by Canadian companies.

Such adjustments in the present tax structure applicable

to fire and casualty insurance would no doubt yield additional funds to the treasury and would distribute the burden of the tax fairly among all insurers, stock and mutual. The stock companies being profit-seeking organizations would pay a profits tax and the mutuals would bear their share of taxation through a uniform premium tax. The cash mutuals would favour such a readjustment even if the premium tax made uniformly applicable to all insurers had to be raised above the rate the cash mutuals now pay.

Submissions

The cash mutuals therefore submit that the Commission should find and recommend:

(a) That the premium tax under the Special War Revenue Act is inequitable and that it is in the public interest to amend that Act so as to impose a premium tax at the same rate upon all fire, casualty and marine premiums paid either within or without Canada on Canadian business, whether written by stock companies (be the same domestic, British or foreign) or written by mutuals (domestic or foreign and however operating, whether on cash or premium note basis and including farm mutuals) or by reciprocals, to the end that all premiums paid by the public in Canada will reflect the incidence of the same tax.

(b) That the Income and Excess Profits Tax Acts as now enacted and administered are unfair to Canadian stock companies and that such Acts should be amended so that Canadian companies will not be penalized because of being Canadian companies while British and foreign companies escape liability for tax upon income derived from profits on Canadian business and heretofore withdrawn to foreign head offices so that Canadian companies pay on large amounts of investment income and British and foreign companies pay little or nothing on

investment income.

(c) That it is not in the public interest to apply or attempt to apply the Income Tax and Excess Profits Tax Acts to cash mutual companies because

(i) The mutuals being non-profit organizations do not fall within the principles upon which the said Acts are based which could only be applied to cash mutuals by an artificial and unwarranted definition of "profits".

(ii) Additional tax burdens should not be imposed on the cash mutuals as they perform valuable public services, namely:

they provide fire and other insurance with complete security to a large part of the farming community and unprotected areas such as small towns, villages and other small rural communities which are not served by fire protection:

they are independent and are not members of or under the control of the Canadian Underwriters Association which controls the business of and fixes rates for its members and as independents the cash mutuals tend to prevent unwarranted increases in the cost of fire and casualty insurance to the public.

(iii) The incidence of excess profits tax on the business of stock companies cannot be shown to have affected the volume of the stock companies' business or to have created a competitive situation so far as the stock companies are concerned; its only effect has been to drain off the stockholders' excess wartime profits. These profits do not reflect themselves in increased cost of insurance to the public.

(iv) While income and excess profits tax do not reach the mutuals this does not make their competition unfair.

(v) The imposition of profits taxes on the mutuals would not contribute any substantial amount to the public treasury

which could be augmented much more generously by amendments to bring under tax liability the investment income of British and foreign companies which now escapes although these companies enjoy the larger portion of Canadian business.

(vi) The imposition of income and excess profits taxes on the cash mutuals could only result in more severe competition to the stock companies.

The cash mutuals request the right to file a supplementary brief in elaboration and support of the representations herein contained and in reply to the allegations and material which may appear in any adverse submissions filed, and in particular in submissions or briefs filed on behalf of the stock companies or any of them or on behalf of the Canadian Underwriters' Association.

All of which is respectfully submitted.

The Gore District Mutual Fire Insurance Company

The Economical Mutual Fire Insurance Company

The Waterloo Mutual Fire Insurance Company

The Perth Mutual Fire Insurance Company

by their Counsel,

N.S. Robertson.

DUNCAN McINTOSH,

General Manager, Gore Mutual Fire Insurance Company, having been duly sworn, deposed as follows:

BY MR. ROBERTSON:

Q. Mr. McIntosh, you are the general manager of the Gore District Mutual Fire Insurance Company? A. Yes, sir.

Q. Its head office is at Galt? A. That is right, sir.

Q. How old a company is it? A. It was established in 1839, so it is 106 years old.

Q. I have shortly described the way you carry on business? A. Yes, sir.

Q. Would you please amplify that? A. Yes, sir. In 1839 we were organized as a mutual company under the act of 1836. At that time all our premiums were taken in arrears. The losses and expenses at that time were added up at the end of the period and divided amongst the members. This continued until 1868 when, through an act of parliament of the province of Ontario, what is now known as the cash mutual organization was created. At that time the company was permitted to operate both on the mutual plan as well as the cash plan. The cash plan is operated under the system of collecting a premium at the first and not at the end of the period. At the same time we were permitted to carry on mutual insurance, with the use of a premium note, and we still carry on that type of business. The premium for the premium note is also paid for the first part of the period, but our dividends are paid on our mutual policies at the end of the period. The cash policy is exactly the same as the policies issued by the life insurance companies, particularly the Mutual Life Company, who issue a non-participating policy. The purchaser of a non-participating

policy receives in effect his dividend at the time he pays his premium, in the form of a lower rate. The mutual member pays an initially higher premium but, according to the act, is a member of the company and therefore is entitled to a dividend which is declared by the directors at the end of the period.

Q. Mr. McIntosh, you heard me report to the commission that in a general way you carried on similarly to the stock companies. Would you elaborate on that? I do not happen to have one of your policy forms here, but I have one of the Economical. Does yours vary much from that?

A. They are identical.

Q. Would you just elaborate, for the benefit of the commission, on just how you carry on your business?

A. Since 1839 the mutual companies, the four cash mutuals, have operated through an agency system. That is, they appoint agents in exactly the same method and manner as joint stock companies. They pay them commissions; they incur largely the same expenses, and we are at all times in direct competition with the joint stock companies, as of course they are in direct competition with the cash mutuals. Does that cover your point?

Q. Yes, I think so. You heard the references I made to the statute requiring that your surplus be maintained at two per cent?

A. That is right.

Q. And that is the fact? A. You will find that in the statutes of the province of Ontario.

Q. What about your rates for insurance, and your rates for commission? A. Well, the growth of mutual insurance I think answers that question, sir. It is hardly likely that, operating through the same agency set up and under the same conditions as the joint stock companies --

Q. Just elaborate on that. You say, "through the same agency set up"? A. Yes. , Quite frequently in the province of Ontario, where a large part of our business is centred, we are represented by agents who at the same time represent joint stock companies.

Q. Agents are agents for joint stock companies and agents for you? A. That is right.

Q. And what conclusion do you draw from that, as to your rates? A. The conclusion we draw from that is that over the years the rate of the mutual company must of necessity have been lower than that of the joint stock company, since the remuneration offered by a mutual company to the agent is, on the whole, not as great.

Q. Is it a fact that over the general field your rates are lower than those of the stock companies?

Q. Quite true.

Q. And is it also true that your commission rates -- how do they compare? A. On the whole, lower.

Q. Now, you have been sitting and listening to the proceedings. What have you to say about your investment income? A. Well, referring to investment income ---

THE CHAIRMAN: I think, Mr. Robertson, that you have made your argument clear on that point. The witness might confine himself more to the facts.

BY MR. ROBERTSON:

Q. Then, to use a common term, one which everybody questions, but without being condemned or damned for using that term, what do you do in respect of underwriting gain and surplus and investment income? What do you do with respect to those three items? A. We have two responsibilities. First of all we have to ---

Q. What do you do? I am not speaking about your responsibility. What do you do? A. In effect we lower the rate of the premium for insurance. That is the result.

Q. Well, in your answer you are starting at one point and jumping to another. Follow it through, if you do not mind. At the end of an accounting period -- and do not let us get into an argument about that -- but at a certain time you take account of what you have done over a period of time? A. Yes.

Q. An annual accounting. A. Yes.

Q. What do you do with underwriting gain or loss, and investment income? What do you do, physically, with those things? You start with certain items, and make subtractions, and get certain results. Then, what do you do with those results, just to follow the process through?

A. If I can follow your question, I shall endeavour to make a short statement on it. However, I am not quite certain as to what you have asked.

Q. Well, I admit I have not made my question very clear.

MR. PARKER: Perhaps a statement of the accountant would be more helpful, would it?

BY MR. ROBERTSON:

Q. Have you a balance sheet here?

MR. PARKER: That is really what you are asking him to do, is it not? You are asking him to summarize?

BY MR. ROBERTSON:

Q. I am asking you to tell the Commission what happens in your company at the end of the year, and where the money goes. Relate your remarks to underwriting gain or loss, or investment income. A. There is a balance, either debit or credit, in respect of insurance. There is income which is derived from the investment of our income - of our investment, rather. These two funds are pooled together, and the necessary reserves are set up, and the balance goes, in the first instance, to the payment of dividends to the mutual policy holder, and to a further reduction in the cash rate to the policy holder who has a non-participating policy. Is that what you wish?

Q. I think so, briefly. It does not, however, go into detail as I might like to have it. But possibly someone at a later stage will give us that. You have said that some of it goes to surplus. Why does any of it need to go to surplus? Why do you put it to surplus? And, further, how much goes? A. Well, as a minimum, we would have to keep our surplus and reserve of at least 2 per cent of fire insurance in force. That is the basis of that. It springs directly from an Ontario statutory condition which requires that procedure. And

against that you must superimpose the cash that each individual company has with what its liability is, and what type of liability it has.

BY THE CHAIRMAN:

Q. You use the words "surplus" and "reserve" in the same sense? A. Yes, in the insurance account the only statutory reserve required is a reserve for a return on unearned premiums.

BY MR. ROBERTSON:

Q. What has been the growth of your reserve, in relation to your insurance in force? A. Very close.

Q. Has it gone parallel with the increase in insurance? A. Yes.

Q. What about the competition your companies have received from the stock companies? Then, further, what about the competition which you give to the stock companies? A. Well, of course, it is like our poor relations; it is always with us. But on the whole I think our competition in our mutual companies with the joint stock companies has been fair. There competition with us, naturally, has been somewhat prejudiced. We have been exposed to the same propaganda as was mentioned yesterday by Mr. Gruhn. However, we take that as part of the business, and we have no objection to competition. I believe the facts with respect to mutual insurance speak for themselves.

BY MR. PARKER:

Q. In other words, you play fair, and the stock companies do not? A. No, I do not say that.

Q. That is really what you have said, is it not? A. No, my friend Mr. Ham would not agree with that.

Q. You do not mean it that way, I understand? A. No, not in that way at all.

Q. You both play fair, is that correct? A. We attempt to.

Q. You take money in? A. Yes, we do.

Q. From a number of sources? A. Yes.

Q. You take a cash payment when you write a participating policy? A. Yes, that is correct.

Q. You take cash when you write a participating policy, a full premium? A. Yes.

Q. And you take cash, or receive cash, from income on investments? A. Yes, that is correct.

Q. And you pay losses? A. Yes, that is correct, too.

Q. And you pay general expenses? A. Right.

Q. Including agents' fees and all that sort of thing? A. Yes.

Q. And you set certain sums in reserve? A. Correct.

Q. What I wish to know is this: in making up the reserve, are they divided -- that is, are they divided in respect of the amounts set aside out of participating policies, and from the non-participating, or are they all put together as a single reserve? A. They are all put together as a single reserve.

Q. And do you put into your reserve the same percentage of non-participating full premiums as you do of the participating cash premiums, to be followed later by an assessment? A. Yes; and, just to correct that point, it does not follow that an assessment follows after the original.

Q. I know, but it might follow? A. Yes.

Q. It sometimes follows. A. It has not in our company.

Q. Never in its history? A. Not since the cash mutual plan was adopted in 1868.

Q. Not since the cash mutual plan was adopted?
A. No.

Q. In making your investments out of that reserve do you keep the separate account of the investments originating out of non-participating policy premiums and participating policy premiums? A. No.

Q. Can you tell me how the holder of a participating policy can ascertain his share in the reserve, or does he also share in the reserve as made up from the two sources -- that is, coming from the participating and non-participating premiums, as well as his own? A. It is a total protection for all policy holders, whether it is a cash policy holder or a participating policy, or non-participating policy. And it is not possible for a participating policy holder to determine at any time what share of the reserves or assets of the corporation are his.

Q. Are the respective interests of the participating policy holders and the non-participating policy holders in those reserves the same? A. No.

Q. What is the difference? A. According to the Ontario Act, and it is the same anywhere, the mutual policy holder is, in effect, the ultimate owner of the company.

Q. Oh, I understand that; but, coming to the point, are those interests the same? I asked before if the respective interests of participating policy holders and non-participating policy holders in the reserves are the same, and you answered that they were not. Is that correct? A. That is correct; they are not.

Q. They are not the same. A. No.

Q. Well, will you tell me the difference between the two? What are the interests of each, and how are they ascertained? A. In exactly the same way as a non-participating policy holder in a life insurance company has no interest in the earnings of the corporation, other than the premium that he pays. To the same extent the cash holder in the cash mutual policy has no further interest in the earnings of the cash mutual company.

Q. I do not know whether that is quite clear, but perhaps I can put it this way: are you saying, in effect, that the interests of all policy holders cannot be ascertained until the company is wound up; is that what you say? A. That is quite true.

Q. And that is a fair way of putting it? A. Yes, that is fair.

Q. And in winding up or going out of business, and in making these reserves ready for distribution, how will the participating policy holder share as compared with the non-participating policy holder? Will they share on the same basis, or do they share on different bases? A. They would share on different bases.

Q. What is the difference? A. The difference is this, that the participating policy holder is a member of the corporation, and therefore he is entitled to his participation in its assets, if the company were wound up. The non-participating policy holder is not a member of the corporation.

Q. He would have no interest? A. No, he would have no interest.

Q. And yet, a portion of the premiums paid by the non-participating policy holder through the years goes

into the reserve, which ultimately goes out to the benefit of the participating holder. A. It could.

Q. Is that the way it works; is that the result -- or is that a matter of argument? A. I think it is a matter of argument.

Q. Well, perhaps it is. I shall go back now to some questions asked by Mr. Robertson, and possibly shall ask them in reverse order, before I reach one or two further questions of a different nature. You told us that you have agents the same as the stock companies?

A. That is correct.

Q. And in some cases, and I dare say in quite a number of cases, the same agent in a village or town -- and this would apply in all fire insurance agencies -- can write a policy in a dozen different companies.

A. That is correct.

Q. In mutual companies and in stock companies.

A. Yes.

Q. All right. Now, a stranger goes into this agency wishing to secure insurance. Do you know what the practice is? How does the agent decide whether he will place the business in the stock company or in the mutual company? A. I should think that in that case ---

Q. Well, do you know, to begin with? A. I think I know the practice.

Q. Well, then, tell us the practice. A. All agencies have their preferences. Some prefer mutuals and some prefer stock companies.

Q. All agents do. A. Yes, some forms of insurance are preferred over others.

Q. By the agent. A. Yes.

Q. Not the insured person; he does not care a hoot

whether his policy is placed in a mutual or a non-mutual company. A. Some do.

Q. I am talking about those who do not; there are some who do not. A. Quite true.

Q. And in those cases it is up to the agent to switch it to whichever he wishes, to whichever his sympathies are with. A. Yes; and then it becomes a matter of added inducement.

Q. What would those added inducements be? A. Increased commission on the business he places.

Q. Is it not true that the mutuals pay the agents a more generous commission in order to bring them the business? A. No, I think you will find it the other way.

Q. Tell me, if you know. A. The commission ---

Q. Do you know what the practice is? A. Yes, I do, generally.

Q. What is it, then? A. The mutual companies pay lower commissions.

Q. Lower commissions on lower premiums? A. Yes.

Q. Dollar for dollar? A. Yes.

Q. Can you tell me what the inducements are when the applicant has no preference in the matter; tell me how you people get him on your list? A. It is quite possible.

Q. How? A. If he has no preference in respect of his interest in mutual insurance, -- if we had a poor agent in that town we would never receive his business, -- and I mean "poor" from our standpoint.

Q. I have in mind a man who exercises ordinary common sense. Then, if an applicant has no preference in the matter, and the agent could get a bigger commission, why would he not send it to the stock company?

What would induce him to pass it over? A. Maybe he is acting in the public interest. Probably he would be content to place that risk in a corporation which offered the same protection but which might probably be more reasonable in rate structure.

Q. That is your answer; I shall accept it.

BY MR. ARNASON:

Q. Is it possible that there is a lower commission paid by the mutual company? He might think that with the lower premiums charged by the mutual company he might get in more business, and would thereby increase his commissions? A. Yes.

Q. And this to some extent would offset the higher commissions paid by the joint stock companies.

A. That is quite true.

Q. Does that happen? A. Yes, it does.

BY MR. PARKER:

Q. Have you heard an agent say that he has prospered by reason of low premiums and low rates of commission, but that they get a lot more little ones and fewer big ones, with the net result that they get more money? A. Yes, oh, yes.

BY THE CHAIRMAN:

Q. Apparently there is quite a bit of competition for the goodwill of the agent. A. Yes, that is very, very great. That is where all the propaganda springs from.

BY MR. PARKER:

Q. Mr. Robertson suggests that perhaps I should ask you to compare the size of the policies written, both mutual and stock. A. As it applies to cash mutuals, do you mean? That question applies to the cash mutuals,

not to mutual insurance generally.

Q. I am talking about your companies, where you have common agents. A. It is not a question of large risks. Invariably it is a question of comparatively small risks.

Q. In all cases? A. In 99 per cent of cases, probably.

Q. Do I understand that all the policies written by agents are small policies, or only those placed in the mutual companies are small? Do I understand that the big ones go to the stock companies? A. I would say that the large policies are not placed with the cash mutuals. They may go to other mutuals, or they may go to the stock companies.

Q. They do not go to you? A. The portfolio of the cash mutual is not composed of large risks.

Q. All right. At the beginning of your testimony you mentioned that in the early stages of the company you started out with the purely mutual idea. A. That is correct.

Q. It was in 1868, wasn't it, that the company went to the legislature and sought power to do business on the other plan? A. Yes.

Q. That seems to represent a departure of this company from its original idea, namely to serve the farmers and to do ordinary mutual business. How did that come about? Why did they not stay as they originally began? why did they branch out? A. Let me correct one statement Mr. Robertson made a little while ago.

Q. Oh, Mr. Robertson did not make an incorrect statement, did he? A. So far as the Gore is concerned. We were never a farm mutual, in the sense that we were incorporated to insure farm risks, only. We were incor-

porated as a mutual insurance company to insure all manner of risks.

MR. ROBERTSON: I apologize.

THE WITNESS: And that is largely true of the other cash mutuals, too -- although I cannot speak for the Economical. It is not true for the Gore.

BY MR. PARKER:

Q. Anyway, the company started out with the idea of doing business on the premium note plan. A. It was required by law to do that.

Q. It was required by law; that is all they could do. A. Yes.

Q. And after thirty or forty years' experience they found, apparently, that they had good reason for seeking permission to work on the other plan? A. That is quite true.

Q. And they got that permission through statute? A. Yes.

Q. I am wondering why; can you enlighten us on that point? I know that it was long before your day, and also before mine; but have you any idea or any accurate knowledge as to what induced the company to do that?

A. To my knowledge the Department of Insurance in Ontario always have taken a keen interest in mutual insurance, and prior to that time the method of operation placed a heavy burden on the mutual insurance companies in Canada. In 1868 the Superintendent, in the interests of what he thought was mutual insurance, brought in legislation to permit mutual companies to secure premiums in advance.

Q. Well, I do not wish to go into detail in the matter, but are you in a position to show that it was done at the instigation of the government authorities? A. Yes.

Q. Rather than being sought by the companies.

A. It was sought by the companies after the government had put that legislation on the books for that purpose.

BY THE CHAIRMAN:

Q. It brought you closer to 'your competitors, did it not? A. Yes.

BY MR. PARKER:

Q. It was only permissive on the companies; it was not compulsory on the part of the Gore Company.

A. That is correct.

Q. It was only permissive. A. Yes.

Q. And the company, as far as you know, proceeded on that basis, because it helped them in their competition against stock companies. A. Would you repeat that question, please?

Q. They sought permission, and exercised the permission given them, and they introduced that type of business because it enabled them to compete to a greater extent with the stock companies? A. No.

Q. Why did they want to do it on that plan, then? A. In 1868 the conditions of insurance in Canada were entirely different from what they are today.

Q. Well, I do not remember that far back, but I shall take your word for it.

THE CHAIRMAN: I do not think you were there then.

THE WITNESS: I was not there, but the records are open to see.

BY MR. PARKER:

Q. What made it desirable for them to get into this new type of policy? A. It offered a greater degree of stability.

Q. Are you on solid ground there? Was it stability

the company was looking after, or was it greater business?

A. Stability.

Q. If you do not know, just say so. A. I do not intend to lead you astray, but the history of our company leads me to believe that it was a question of stability, purely.

Q. You do not think competition, or action to get more business, had anything to do with it? A. No, not in 1868.

Q. Let us turn to page eight of the brief. I suppose you have read this brief carefully, and assisted Mr. Robertson in the preparation of it? I suppose the statements that are in that brief as statements of fact, as distinct from legal arguments for which we will have to hold Mr. Robertson responsible, are substantially true? A. I believe so, yes.

Q. As I understood Mr. Robertson's argument -- and I do not think this is a question of law that I am putting to you, or at least I hope it is not -- in effect Mr. Robertson said that there is no such thing as profits in this type of business. A. Yes.

Q. That it was a wrong name. A. Yes.

Q. And yet he points out the section of the Ontario Companies Act, quoted on page seven of the brief, and introduced by the following words:

"The cash mutuals accumulated the bulk of their reserves while operating under provincial registry."

I have no doubt that that is perfectly true. Then he continues:

"The Ontario statutes recognized the need of security as is evidenced by section 275 of the Ontario

Companies Act, R.S.O. 1937, chapter 251, which reads as follows" -

Then he quotes a certain section of the Companies Act dealing with reserve. It will be noted that the section says:

"Subject to the provisions of subsection 5, a mutual or a cash-mutual insurance corporation...."

That is your company? A. Yes.

Q. I continue reading from the section:

"....may form a permanent reserve fund...."

It will be noted that it says "may"; there is no necessity, according to this statute, unless counsel argues that "may" means "shall". It states:

"....may form a permanent reserve fund, to consist of such part of the net profits as may from time to time be set aside by the directors for that purpose;"

Now, as I say, I do not wish to enter into an argument as to whether that is a bad thing, or whether it is a proper thing. I thought perhaps you could help me in this. Mr. Robertson also said, as I understood him -- and if I am wrong he will correct me -- that we are entering the field of accountants' language. It may be proper language when talking about accountancy, but the suggestion is that it was improper when talking about taxation. You will agree with me that that is the language in the Ontario Companies Act, at any rate, and the Ontario legislature seemed to think that the word "profit" was the appropriate word to describe certain takings of these companies, did it not? A. According to that Act, yes.

Q. And from your knowledge of economics or account-

ancy, have you any reason to complain that that does not describe the intakes of surplus -- and I do not wish to use the word myself -- the surplus intakings of your company? Have you any quarrel with the words used in the Ontario statute to describe it? A. Yes.

Q. What is your quarrel? A. It is arbitrary. I say the definition of "profits" is arbitrary.

Q. I beg your pardon? A. The definition as to what constitutes a profit is an arbitrary definition.

Q. There is no definition there, as I see it.

MR. GEOFFRION: Yes, I suggest subsection (3) refers to it.

MR. PARKER: It refers to "such part of the net profits". Net profits and profits are entirely different. They are talking about "net profits" in subsection (1).

MR. GEOFFRION: That is the expression used.

MR. PARKER: Oh, yes, I beg your pardon, it refers to net profits. Apparently the definition of "net profits" is not given, is it?

BY THE CHAIRMAN:

Q. What Mr. Parker is asking you is this: why did the Ontario legislature, as late as 1937, use such a condemned word as "profit"? Do you know why? A. No, I cannot say that.

BY MR. PARKER:

Q. I go farther than that: from your knowledge of the workings of your company, are you in a position to say whether it is a suitable word to express what your company does? Have you any quarrel with the use of the word? A. Yes, I have a definite quarrel.

Q. Then, what is your quarrel; what is wrong with it? A. What is profit in our organization is not the

difference between the income received in the form of premiums, and the losses and expenses. For us, we feel in the same way as the life insurance companies do, that interest from investments is an integral part of the premium.

BY THE CHAIRMAN:

Q. You operate either at a loss, at a profit, or exactly at cost? A. Or endeavour to.

Q. No, not that; you operate either at a profit, a loss, or break exactly even? A. That is correct.

Q. You have not been running at a loss, have you? A. No.

Q. Have you been breaking exactly even? A. I would say that would be impossible.

Q. Then, there is a profit? It may be very small, but you cannot get away from that? There are only three situations under which any company can operate, and those are the three I have named - loss, profit or breaking even. A. That is construing that what remains over after you have paid your losses and expenses is a profit.

Q. I am referring to the Ontario statutes.

BY MR. NADEAU:

Q. Do you operate outside of Ontario? A. Yes, we operate in all provinces of Canada.

Q. What kind of insurance do you sell? -- casualty, accident and fire? A. Fire and casualty.

Q. What is the ratio of your participating business as compared with your non-participating business?

A. Probably about 10 per cent.

BY MR. GEOFFRION:

Q. Which is 10 per cent? A. Ten per cent is participating; that is approximately correct.

BY MR. NADEAU:

Q. For all your companies? A. No, that is for my own company.

Q. For your own company? A. Yes.

Q. You do not know about the others? A. I could answer that, but I think the manager would be in a better position to answer it than I am.

BY MR. ARNASON:

Q. Is it the objective of your company to operate at cost? A. Yes, definitely.

Q. Is it possible there may be certain elements of cost which cannot be determined accurately at any time? A. Yes.

Q. And that may explain the prevalence or the accumulation of what may be termed part of your surplus? A. Yes, definitely.

BY MR. PARKER:

Q. Do I understand you to say that that means that 10 per cent of the number of policies issued are on the note plan, and about 90 per cent on the cash plan?

A. About 10 per cent of the amount of fire insurance.

Q. In dollars? A. Yes, in dollars.

Q. So that 90 per cent of your business is done in every respect on exactly the same basis -- that is, the writing of it -- on exactly the same basis as that of stock companies? A. Yes.

Q. And the only difference between you and the stock companies is the way in which you deal with earnings after you get them? A. That is correct.

Q. Coming back to this definition of profits -- and I do not wish to labour the point too far, but as my learned friend pointed out, net profit as defined in

this section -- and Mr. Robertson has been good enough to furnish me with the Act and the section -- there seems to be no definition of the term in the section. I cannot find it.

MR. ROBERTSON: I cannot, either.

THE CHAIRMAN: To what does it refer? To what section does it refer?

MR. ROBERTSON: I had quoted the section only in reference to the 2 per cent. I had not addressed myself to the definition of "net profits" at all.

THE CHAIRMAN: Is 251 contained in any section or chapter of the Act?

MR. ROBERTSON: It is in the Companies Act. I was just looking to see if it was divided into sections.

MR. PARKER: It is section 275 of chapter 251.

MR. ROBERTSON: I would refer to part 16, but I have not combed through it to see if there is a definition. However, I shall do so in the next few minutes.

MR. PARKER: We will let it stand, then. That leaves the brief somewhat in the air, because it throws us back on our own to find out what "net profits" means.

MR. ROBERTSON: There are these descriptive headings which are not marked as sections, or anything else. It is a point into which I have not yet examined. However, I shall see if I can look into it.

BY MR. PARKER:

Q. One other thing: you heard Mr. Robertson, in his presentation, speak about underwriting profits?

A. Yes, that is true.

Q. He placed it before the Commission on the basis that underwriting profits mean money going into one's pocket, fresh, as distinct from -- I forget the other

expression he used.

MR. ROBERTSON: Savings.

BY MR. PARKER:

Q. I believe he referred to keeping it from getting out. The income which the company receives from investment of its reserves goes into the company's pocket; it is not just a scheme devised to keep it in its pocket, or to prevent it from getting out of its pocket. It is exactly what Mr. Robertson described, a means of acquiring money and of having it flow into the company's pocket. Is that not correct, in respect of investment income? A. Is that a legal argument?

BY THE CHAIRMAN:

Q. In the hands of anybody else but mutuals, investment income would be profit? Why in your case is it not the same? A. Because in one case it goes to the shareholders.

BY MR. PARKER:

Q. That is what you do with it afterwards?

A. Yes.

Q. I am talking about it as it goes into your pocket. You may take it out of your pocket and go on a spree with it, or do what you like with it, but ---

BY THE CHAIRMAN:

Q. Put it this way: it is your contention that the tax gatherer must look at the ultimate destination of the income to determine what it is? A. I should think so, yes.

Q. That is an argument we hear frequently.

BY MR. PARKER:

Q. I call your attention to page 316 of the blue book for 1942, where certain information concerning your

district is tabulated in your profit and loss account for the year. Interest and dividends earned in that year were \$122,650.45? A. Yes, that is correct.

Q. And gain on the sale of investment; you even make capital gains on those investments? A. That is correct.

Q. And you also, in another year, may probably make a capital loss? A. Yes.

Q. I appreciate that, of course. Whereas your underwriting gain is only \$14,000, your interest and dividends earned is \$122,650.45. A. Yes.

Q. And yet this company has no profits in the sense that nothing goes into its pockets. A. You are trying to distinguish between what goes to the company from the standpoint of ---

Q. They both go to the pockets of the company. A. Yes, but one is not in any sense a profit, as compared with the other.

Q. We have heard that before. Then, at page six of the brief a statement is made which I shall bring to your attention. I do not see the point of it, myself, but perhaps counsel who helped prepare the brief may help me. You set out the amount of dividends which stock companies have drawn over the last number of years? A. Yes.

Q. I believe you go back for thirty-five years? A. Yes.

Q. I suppose that is put in the brief to leave the impression of what profiteers, literally, these stock companies are; is that why it is put in there? Or, do you know why it was put there? A. I would not say that.

Q. You would not say that? A. No.

Q. There are no figures inserted in the brief to show the number of millions or tens of millions of good, solid capital that has been invested, on which that was earned, and have not shown as to whether these public malefactors, these shareholders, got 2 per cent on their investment, or 50 per cent? There is no information furnished on that score, is there? A. In this brief?

Q. Yes. A. No, that is quite true.

Q. Have you any idea of whether that point was considered in the preparation of the brief, or whether it would be a good idea, having shown the profits of the stock companies, to show how much honest-to-goodness capital they put in, risked and ventured in the business? A. I do not think I see your point, at all.

Q. Well, I shall not press it further. Then, your counsel drew an analogy with respect to trustees. You heard him say that the company was in a position of trustee for these reserve funds? A. Yes.

Q. And that the company held them, in effect, if not in form, as trustee for the policy holders; is that correct? A. Yes, that is true.

Q. Where is there any trusteeship? Is there any by-law, or anything indicating trusteeship?

MR. ROBERTSON: Is not that purely a legal argument?

THE CHAIRMAN: I think it is, possibly.

MR. PARKER: If my learned friend leaves it on that ground, I shall withdraw the question.

MR. ROBERTSON: It is a matter of analogy of operation.

MR. PARKER: Then, one other question in respect of personal corporations.

BY MR. PARKER:

Q. Are you familiar with the Income War Tax Act, at all? A. Yes, but not in its legal sense, in the way that is brought up.

Q. I am not going to ask you to interpret it at all; but in order that the record may be straight I wish to know if you are familiar with section 21, subsection 9. I might point out that section 21 is the section dealing with the way personal corporations are taxed. As the Commission knows, the taxes are passed on to the shareholders, except in the case of non-residents. Then the last subsection reads:

"That the rates of tax applicable to corporations, as in this Act provided...."

That is the general corporation tax --

"....shall be payable by a personal corporation on that portion only of its income which is deemed to be distributed to non-residents."

In other words, even in respect of a personal corporation, the corporation itself is the taxpayer and pays the amount. I cite it merely to show that you do not wash the whole thing out.

THE CHAIRMAN: That is to meet Mr. Robertson's argument.

MR. PARKER: In order that it might be brought to the attention of the Commission later on, so that it will not be overlooked.

MR. ROBERTSON: It is against the argument with respect to the corporate entity of the company. That is all it is directed to.

BY MR. ROBERTSON:

Q. There is a suggestion that we have failed to

show these colossal and astronomical sums invested. I would direct the attention of the Commission to the second last paragraph on page fifteen of the brief, and would also ask the Commission to look at the 1942 blue book, page 107, and see if the amounts of invested capital appear in the brief. Possibly it need not be read.

THE CHAIRMAN: Your reference to it is sufficient, Mr. Robertson.

MR. ROBERTSON: The last column shows capital stock paid in cash, and there is a cross-reference in my brief to the page in the blue book. We show an increase in capital and invested assets every year.

BY MR. ELLIOTT:

Q. What part of the business of your company is fire, and what part is casualty? A. About four-fifths is fire.

Q. And, of the fire business, what proportion of the risks are written in unprotected areas -- that is, areas without fire fighting apparatus? A. On an estimate I would say about 70 per cent.

Q. Can you distinguish between farm risk and other risks in unprotected areas? Can you tell me how much of that is farm risks? A. In our own company?

Q. Yes. A. Maybe about one-sixth of it.

Q. One-sixth of the total fire business? A. Yes.

Q. Then, in computing your net premium for the purpose of premium taxation, how do you proceed?

A. Until 1943 the dividends which had been paid had been permitted by the department to be deducted. I believe this matter was mentioned by another mutual. In 1943 we were ordered to pay a premium tax on all the dividends paid since 1932 or 1933. We forwarded to the

treasury the required sum. Apparently, however, some companies took objection to that, and the amount was returned to the companies with the notation that that change would be in effect in so far as 1944 was concerned. So that, so far as 1944 is concerned, we paid the premium tax on the total premiums received before any dividends were paid.

BY MR. VAUGHAN:

Q. When you referred to the tax being the same in all, that is both in joint stock companies and in mutual companies, would your idea be to compute that on the gross premiums? A. Yes, we feel that is the most equitable basis to tax all insurance premiums.

Q. On gross premiums? A. Yes.

BY MR. PARKER:

Q. You said about 10 per cent of your insurance is participating, and about 90 per cent non-participating? A. Yes.

Q. I was wondering why that is so. A new person comes to your agent and asks to be insured. How is it divided, or who decides whether he will be given a participating or non-participating policy? A. I should be glad to explain that.

Q. I wish you would, because there might be an impression left that there is some inducement made to keep it out of the participating group. A. Quite true. I believe Mr. Gruhn mentioned that point yesterday. Since the time of incorporation it was necessary to sign a premium note. As this company grew, and the number of stock companies increased, we had what we now know as non-assessible mutuals -- that is, mutuals which can sell mutual policies which are not subject to extra assessment in the event of great loss. But, under our

Act, we were not permitted to issue policies except with the premium note. Naturally, as the result of a considerable amount of propaganda aimed at the Canadian mutuals, a body of the Canadian people would not sign premium notes -- and they will not sign premium notes today.

Q. Is it carefully explained that if they do they will participate in these big reserves some day, and that if they do not they will not participate? A. That argument still does not seem to have convinced a great many of them.

Q. Is the argument made? A. Yes, -- not made in the sense that they will participate in the splitting of some big melon, because there is no anticipation that a large company and a going concern will wind up.

BY MR. ELLIOTT:

Q. Do you issue casualty policies on participating insurance? A. No, we have just started in the casualty business -- started about four or five years ago.

Q. You do not offer participating insurance?
A. No, not in casualty.

Q. And therefore the 10 per cent of total business is a larger proportion of your insurance business ---

A. It is 10 per cent of our insurance business.

BY MR. VAUGHAN:

Q. What is the rate of your rebate to your participating policy holders? A. Twenty-five per cent for the last fifty-five years.

BY MR. ELLIOTT:

Q. What is the difference between payment on the participating premiums and similar cash premiums?

A. On a close estimate I would say about 10 per cent. That is, a man who takes a mutual policy and receives a

dividend will probably pay a premium 10 per cent below what the cash policy holder would pay.

BY MR. VAUGHAN:

Q. That is 35 per cent altogether. A. No, he gets 10 per cent less to start with, and then he gets -- well, it is not exactly 35 per cent, but --- A. In the initial stage the mutual policy holder pays more.

Q. He pays more? A. Yes.

Q. Ten per cent more, probably? A. It would be considerably more than that, because after he receives 25 per cent dividend, or whatever it is ---

Q. What would be the net difference? A. Ten per cent, I would say.

Q. Then, one further question as to the point of these companies acting as trustees. Do you see any difference between those companies acting as trustees, and the banks, which hold very large deposits for their depositors, and are responsible for the investment and care of funds? A. I do in this sense, that there is a body of people at the top of a bank, in the form of its shareholders, who are receiving profits from that banking organization.

Q. Well, if there were not such high taxes to pay, perhaps the depositors would get more benefit, too.

A. They might; that is a question for the banking authorities to consider.

Q. It is quite logical, is it not? The rates have been cut down in the banks, and taxation has been heavy. It is logical, is it not, that the depositors probably have suffered to some extent by high taxation?

A. Quite true.

Q. I just wondered whether there was any very

distinct difference between the two, because I would say the banks are really trustees, to the same extent as the insurance companies. A. Certain types of insurance companies.

The Commission adjourned at 12.35 p.m.

Ottawa, Thursday,
April 19, 1945.

The Commission resumed at 2.15 p.m.

Examination of Mr. McIntosh continued.

BY MR. ROBERTSON:

Q. There is only one question I think should be asked by me of Mr. McIntosh, to possibly clarify his answer. In reply to a question by Mr. Parker, Mr. McIntosh, as to your company's position in regard to the imposition of the premium tax on gross or net premiums, what was your answer; do you remember? A. Was that a question by Mr. Parker or by one of the commissioners? I believe I stated at that time that it was my opinion that the tax should be on the basis of the gross premiums. I feel that in considering that question in the light of all mutuals -- I was thinking strictly in terms of my own company at that time, but it makes so little difference that I automatically said "gross." Considering all the activities of the mutuals, I feel that the premium tax should be imposed on the cost of the insurance to the assured. That would be, in the case of the majority of the mutuals, the gross premium which the assured paid, less his dividend which he was allowed. That would be the net cost to the assured.

BY MR. PARKER:

Q. May I just ask this one further question on that point. To clear that up, Mr. McIntosh, when you have a meeting of your members to elect directors -- you have directors, have you? A. Yes.

Q. The only persons who meet to elect the directors are the participating policy holders? A. That is true.

Q. They have the entire control of the affairs of the company? A. That is right.

Q. And 90 per cent of your policy holders have nothing to do with it? A. That is right, sir.

BY MR. HAM:

Q. May I be permitted to ask you a question or two, Mr. McIntosh, or possibly more than that? Does the Gore Mutual belong to either the Independent Fire Insurance Conference or the Independent Automobile Conference? A. They do, sir.

Q. And in the membership of that conference there are mutuals and joint stock companies; is that not a fact?

A. That is quite true.

Q. You stated this morning that one of the competitive advantages you had was lower premium rates and lower rates of commission. Is that correct? A. I believe I said the competitive advantage was lower rates, and in some instances it naturally followed that the lower rates would bring about a lower commission.

Q. Did you mean the commission percentage-wise, or in actual dollars? A. In actual dollars.

Q. Because I would refer you to the Blue Book. I am afraid I am in a worse position than Mr. Robertson, because I cannot even read the Roman numerals, but I think it is on page 126, where it says that the Gore District rate of commission and brokerage, per cent of premiums written in all companies, would be 25.46? A. That is true.

Q. That the average rate of commission for all companies, including the Gore, was 24.40 and 24.74; one figure is for 1942 and the other is for 1941. Might I ask if you operate through a general agency anywhere in Canada? A. In one province.

Q. Which province is that? A. British Columbia.

Q. The rest of the business would flow through local agencies, so-called in the business? A. True.

Q. Would you agree that a general agent operating for a province would receive a higher rate of commission than a local agent reporting direct to you? A. That has generally been considered so, as you know.

Q. So that the rates of commission disclosed there, with you having just one general agency where the commission rate is higher because of supervisory service, is set off against a number of companies who might operate in three, four, five or seven or eight provinces on a general agency basis; and therefore their commission level would be higher, for the supervisory services, and would be reflected in those figures?

A. Yes; but might I answer that question by pointing out that the figures which you speak of now do not reflect the true commission which is paid in the field to agents. In those figures you will find the question of re-insurance, and the rates of commission paid on re-insurance, as you well realize, include quite an item of cost. Is that not so?

Q. Re-insurance commission is included in those figures?

A. Yes, I think you will find it in all cases, even in the case of the stock companies.

Q. That is the commission cost, as I read it: "the rate of commission and brokerage, percentage of premiums written." You claim that includes re-insurance commission?

A. Oh, definitely, yes.

Q. That can be dealt with in argument; it can be ascertained later. This morning Mr. Robertson made reference to the Wartime Prices and Trade Board, in regard to your brief, and suggested that the agency agreement might possibly be a violation of that. Do you, in dealing with your agent,

consider him to be an employee? A. Definitely not.

Q. He is an independent contractor, in your judgment?

A. Definitely.

Q. In following the evidence this morning I am not quite clear whether you have two classes of policy holders, or three. You have an assessment policy holder? A. True.

Q. Then you have a participating policy holder. Is that the same thing? A. That is the same thing.

Q. It is the same; so there are really only two?

A. Yes.

Q. Those on assessment get a dividend, and the others are non-participating, as you suggest? A. True.

Q. And I think you said this morning that only those on a participating basis have a right to vote at meetings?

A. That is true.

Q. So those on the assessment basis actually offer to the public a contract of insurance which may be purchased by the public generally, who are not members of the company. Is that correct? A. Would you repeat the question so I can follow it?

Q. Perhaps I will restate it in this fashion. A non-participating policy holder is not a member of the company?

A. That is true.

Q. Have you any idea how many members or assessment policy holders you have in round numbers? A. Sixteen hundred.

Q. And what percentage of those members would attend an annual or general meeting, roughly? A. Roughly, 50 to 60.

Q. Fifty or sixty individuals? A. I might explain that for your advantage. After the inception of the cash mutuals, including our own, their operations were chiefly

confined, for many years, to south Waterloo, so a great number of the original policy holders are still in that section, and they are quite anxious to see that we do not step out of line.

Q. And can assessment policy holders vote by proxy?

A. Oh, yes.

Q. They state who the proxy is to be? There is not any by-law which says any one individual shall be the proxy in the event of the member not attending? A. That is quite true.

Q. The member designates his own proxy, if he so desires?

A. Yes.

Q. What notice is required of a general meeting?

A. Notice of the annual meeting, or any meeting, must be sent in writing to each member fifteen days in advance.

Q. Prior to the meeting? A. Yes.

Q. From time to time you obtain new members, and from time to time you lose old members, so that your membership, even among the assessment policy holders, is somewhat fluctuating? A. True.

Q. And as membership depends upon the holding of a policy, the right of cancellation of a policy can terminate membership, as such? A. That is true.

Q. With respect to business written, do you write business outside of Canada? A. We do, by way of reinsurance only.

Q. And with respect to the business that you write, have you any conception -- you say in your brief you write 16,000 farm risks. In the brief presented by the Ontario farm mutuals they say that in Ontario they write 140,000 farm risks; and in all the provinces of Canada you write something like 16,000. Have you any idea of what 16,000

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farm risks would amount to in relation to the total, what ratio it bears to the farm insurance in Canada? A. You mean our proportion?

Q. Your proportion of the total farm business in Canada?

MR. ROBERTSON: In all the cash mutuals, or just the Gore?

MR. HAM: All right; all the cash mutuals, if the witness can tell me that. If not, he can tell me about the Gore.

THE WITNESS: As a whole, 16,000 farms would constitute a very small part of the whole farming community of the country.

BY MR. HAM:

Q. It is not a substantial part of the farm risks of Canada? A. No.

Q. In his argument this morning Mr. Robertson made reference to the marine business, and said that the companies which compete with you were in the marine business and, because of the tax situation with respect to them, they were your competitors in the fire and casualty business and being free of taxes on marine business were in a better position to compete with you. Do you support that statement? A. From the information we can obtain from the Blue Book, I would say yes, that would be so. If it is not so it must be because there is information withheld from the superintendent's department. I do not mean to suggest that any such information is withheld with any intent; I mean it does not appear in the Blue Book.

Q. Do you suggest that all your joint stock competitors are in that position? A. Oh, no; not at all.

Q. You have not any idea how many of your joint stock competitors are engaged in the marine business and fall within the ambit of Mr. Robertson's observations this morning?

A. I would answer that question by just saying that it is to our certain knowledge that there are stock companies in the marine business who are in competition with the mutuals.

Q. But certainly not all the stock companies? A. Oh, definitely not.

Q. It is stated in the brief, I think on page 4, that it is an accepted fact that mutual rates have been consistently lower, and I think that point was emphasized by Mr. Robertson this morning. What facilities have you for knowing what the joint stock company rates are? A. Oh, we have no facilities for knowing those rates; but our proof that the statement is correct arises from the fact that mutual insurance has consistently expanded, and more people are insuring in mutual companies; and there is no incentive for a person to insure in a mutual company other than the question of rate.

Q. I think you said you belong to the Independent Automobile Conference? A. We do.

Q. And some members of that conference are mutual and some are joint stock? A. That is true.

Q. Has that conference attempted to maintain rates amongst their members for automobile insurance? A. I will answer that question in this way, Mr. Ham. That conference has attempted to stabilize the rates in the automobile insurance field. Before the inception of that conference the Canadian Underwriters Association was the only organization which had broad enough facilities to bring down any reasonable experience, and we took no exception to the Canadian Underwriters Association for having had that experience. That was

their business; but the independent companies who were experiencing much the same experience as Canadian Underwriters felt that in the interests of the public as well as the insurance companies there should be an association of ideas.

But I want to point this out in the answer, that there is no understanding and no written agreement which binds any member of the Automobile Conference to retain any set of rates. The company is still permitted to give expression to what it considers to be an adequate rate in the case of automobile insurance.

Q. As I understand what you have said, in the Independent Automobile Conference there is no understanding with respect to the maintenance of a rate level on automobile business?

A. There is no written understanding.

Q. But there may be an understanding? A. There may be a voluntary understanding.

Q. The fact is that there is an understanding? A. In effect there is.

Q. With respect to the automobile business, then, that statement does not quite stand, because if you live up to your obligations under that Conference you will charge the same rate as the joint stock members of that Conference?

A. Not necessarily so. There is a differential agreed upon which some of the mutuals enjoy and take into account. Other mutuals deviate from that accepted rate by different percentages. There is no undertaking on the part of any company to strictly adhere to the rates brought down by the Independent Automobile Insurance Conference. In that connection I think Mr. Foot would be probably a better person to give you the information, because he is more closely connected with that organization.

MR. HAM: Then perhaps I will put a question to Mr. Foot with respect to that.

MR. ROBERTSON: And I will put him in the box so you may do so.

BY MR. HAM:

Q. And of course your policies, being like those of the other companies, have a short date cancellation table and penalty? A. That is true.

Q. Do you call it a penalty? There is an excess cost on short date cancellations? A. That is true.

Q. In the event of that being charged against any policy holder, to whose profit or benefit would it inure? A. The policy holders.

Q. To the policy holders? You have two classes of policy holders. Which class? A. Both. To one policy holder a portion of that saving would go in the form of a lower rate. The other, who is participating, will receive part of that saving in his dividend.

Q. Let us take a non-participating policy holder, a member of the public, who insures with you. He carries his policy for one month, then cancels it. You will charge him something in excess of pro rata for one month? A. Yes.

Q. He is no longer a member. Who derives the benefit of that excess of cost over pro rata for the month? A. Well, granting that there is a so-called profit, which I do not agree there is at all; granting there is a profit, that would be transferred to the general income of the company.

Q. And would inure to the benefit of -- ? A. Of the policy holders.

Q. And of course you have investments, and income from investments? A. Yes, sir.

Q. In your brief, at the top of page 7, I wonder if you would explain the statement made there to me. I refer to the second line:

"-- but in every calculation interest is an element in the determination of fire and casualty rates."

Do you support that?

MR. ROBERTSON: Let him read the context.

THE WITNESS: I would prefer that you read the whole passage.

BY MR. HAM:

Q. The whole paragraph reads:

"Indeed an analogous situation exists in respect of life insurance companies. They possess large investments from which they derive income. The investment income is an essential element in the determination of their rates. As the interest rate goes down the cost of insurance goes up, as has happened recently because of the current trend of interest rates to lower levels. Admittedly the principles of life underwriting are, of their very nature, on a more scientific basis than those of fire or casualty insurance but in every calculation interest is an element in the determination of fire and casualty rates."

A. And you ask me if I subscribe to that?

Q. Yes? A. From the standpoint of mutual insurance, yes, definitely; for the simple reason that the income which is derived from the investments is a part of the income.

Q. If that is the fact, then how can your company belong to the Independent Automobile Insurance Conference? One company may have reserves of \$5,000,000 and write identically the same volume of business as another company with reserves of \$1,000,000? A. Yes; but I have already told you that there is no commitment on the part of our company to restrict

our rates to those decided upon by the Independent Automobile Insurance Conference; and if you mention the Independent Fire Insurance Conference -- did you mention it?

Q. No; the Automobile Conference. A. So it does not interfere at all with the principle as we have enunciated it here.

Q. Then you simply make your own rate? A. That is true.

Q. Having taken into consideration the interest from investments? A. Well, we must do that, because that is the basis of our operation.

Q. With respect to the statement on page 8, where you set out the reserves in force in the fire insurance business, would it be possible for you to answer this, or perhaps Mr. Robertson might deal with it. I think it would be interesting if the Commission were supplied with similar figures for the casualty and automobile business of the group. Would it be possible to obtain that? A. That would have to come up as unearned premium. You do not estimate net insurance in force in casualty and automobile insurance in the same way as you estimate the insurance in force in fire insurance.

Q. No; but those figures could be made available to the Commission? A. We must submit that to the superintendent every year.

Q. That would be available; and would you file the figures? A. Definitely, if the Commission so wish.

Q. Then may I refer for a second to the fact that there was an increase in automobile rates in the province of Quebec, due to experience, in which the Independent Automobile Association and the Canadian Underwriters subscribed to the increase, between them; and such increases were advertised in the

province of Quebec. Did the Gore subscribe to the cost of that advertisement? A. I could not say. We do not operate in the province of Quebec.

Q. Very well, that excludes that question. That is the one province in which you do not operate? A. Yes, sir.

Q. In accepting re-insurance, do you limit your acceptance of that re-insurance to mutual contracts, or do you accept it from joint stock companies if they offer it to you? A. We do our re-insurance by treaty re-insurance.

Q. Yours? A. And acceptance as well; re-insurance is both assumed and ceded.

Q. And have you any contracts with joint stock companies? A. We have.

Q. Of course they are not members of your organization? A. That is quite true.

Q. How is your rate of dividend arrived at, to go to the participating policy holders? A. It has been the policy of the board of directors in our company, who have complete authority as to what the dividend shall be -- it has been their policy for the last fifty-five to sixty years to stabilize that dividend. That dividend has been stabilized at the rate of 25 per cent to the participating policy holders.

Q. Is that 25 per cent applied to fire business and automobile business and casualty business generally, or is there a distinction as to the class written? A. The mutual insurance, in our own company, is confined entirely to fire insurance.

Q. You just write fire insurance? A. No; we write all classes, but I say the mutual element.

Q. The dividend only applies? A. Yes.

Q. So it might not be out of the way to suggest that the

participating policy holders in the fire business are, as a group, in the automobile and casualty business? A. Would you repeat that?

Q. That the policy holder members of the Gore Insurance Company, as a group, are in business selling casualty and automobile contracts to the public? A. Oh, no; I do not subscribe to that at all. It would be in effect the same as saying that a mutual policy holder in the Mutual Life is in business selling a policy of insurance to a non-participating policy holder.

Q. I may subscribe to that myself, but I am asking you is it not a fact that the fire policy holders on the assessment plan, as a group, offer to the general public contracts of casualty and automobile insurance? A. No, but I can understand your question on that point. I think it is just a question of having one group who, by law, are accepting a liability. There is no question about that; and there is another group who, from the standpoint of law, certainly are not members of the company.

Q. Of course it is a fact, Mr. McIntosh, is it not, as you stated, that the policy holders in the automobile business are not and cannot be participating policy holders? A. That is true.

Q. So, then, they are not members of the company?
A. They are holders of the mutual policies on a non-participating basis.

Q. They can be policy holders, though? A. Oh, sure.

Q. But not members of the company? A. That is true.

Q. So they are members of the public? A. That is true.

Q. With respect to the fire business, does the policy

holder who has had a loss participate in the dividend, irrespective of the loss? A. Quite true.

Q. In sending out your notices for annual meetings, if I may revert to that for a moment, do you send out proxy forms to members when you send out the notice of the meeting?

A. That is right.

Q. And is there any name suggested on the proxy, as to who might have it? A. Quite frequently there is a letter accompanying it, designating the managing director -- at that time there was a managing director. At the present time, with just a general manager, that letter would have to contain the name of someone on the board.

MR. HAM: That is all; thank you very much.

BY MR. ARNASON:

Q. Mr. McIntosh, with regard to the procedure which Mr. Ham was examining you about, I think you stated that about 60 of your members attended the annual meeting?

A. Yes, sir.

Q. As a rule? A. Yes, sir.

Q. Out of about 1,600? A. Yes, sir.

Q. I am going to ask you a question which may seem rather unusual from the standpoint of insurance procedure; but have your directors ever considered the possibility of amending the by-laws in order to allow your members to appoint delegates to your annual meeting, thus securing a wider representation? A. That matter has been considered and is being considered by our board. As far as the company as a whole is concerned, at the present time we are endeavouring to broaden that very basis, but we are so restricted by the Insurance Act in that regard that we cannot hurry that matter.

Q. Do you mean to say that the Ontario Insurance Act

would tend to restrict the adoption of that policy? A. Yes, in so far as they require the premium note being signed; and we have found it extremely difficult -- I believe my friend Mr. Ham will substantiate me in this -- to get people, irrespective of what the protection is or the financial condition of the company, to sign premium notes.

Q. Another point. I wonder whether you would care to tell us some of the reasons why the non-participating policy holders are not given voting privileges? A. For the reason that they do not accept the liability which a mutual policy holder on our premium note accepts. He accepts a liability to the extent of five times the premium which he pays, whereas the cash policy holder accepts no such liability. That is why, as defined in the statutes, the only person who can vote in the cash mutual company is a man or an insured who signs a premium note.

BY MR. McKENZIE:

Q. Mr. McIntosh, I am particularly interested in the marine business in Canada. I understand that none of your companies write any marine insurance? A. That is true, sir.

Q. I am right about that, am I not? A. You are.

Q. A moment ago you mentioned that you wrote all classes, but you do not include in that statement any marine underwriting? A. That is so.

Q. So your companies are in no way in competition with the marine underwriters? A. That is not so.

Q. No? A. The Insurance Company of North America, for example --

Q. I am speaking now, Mr. McIntosh, of marine companies as such, and marine business as such. You are not in competition with any marine underwriter as such? A. In the marine

business? That is true.

Q. So in so far as any marine rates are concerned, you have no interest? A. That is true.

Q. In so far as any marine underwriter as such is concerned, you have no interest in what taxes he might pay? A. That is true.

Q. And that would likewise apply with reference to any tax on marine premiums? A. That is true.

Q. You have no interest in that? A. No.

Q. Just on that particular point of the exemption from tax on marine premiums, under the Special War Revenue Act, you know as a matter of fact that marine premiums are exempt, do you not? A. That is true.

Q. Do you know the reasons why they are exempt? A. No, I do not.

Q. Then there is just one other point, and it is with reference to your submission contained on page 24 of your brief, where you suggest that it is inequitable that marine premiums do not pay any tax. With reference to marine underwriters and your business, that would not concern you at all, would it? A. I would not answer that question in that way. I would answer it in this way. Man does not live by bread alone, and insurance companies do not live by the premiums which they derive from the fire insurance business alone. They live by the premiums they collect for all classes of business; and when any group of insurance companies, whether they be in fire insurance --

Q. I quite appreciate your point, but I do not want to take up the time of the Commission in that way. A. I just wanted to answer the question in a proper way.

MR. ROBERTSON: Let him finish the answer. You may not

want him to do so, but I think he should be allowed to finish the answer he started to give.

MR. McKENZIE: I quite agree.

MR. ROBERTSON: Do not ride him out to the rail, in other words; let him finish on that point.

BY THE CHAIRMAN:

Q. Finish your answer, Mr. McIntosh. A. I have almost forgotten it. The point is this, that when an insurance company is an insurance company, whether it writes fire, casualty, life or marine, the life of that company depends upon its income. That income may come from any classification; and if you want to apply taxation similar to the suggestions before the Commission at the present time, then it should not be possible for one insurer to make a profit on one classification and make a considerable underwriting loss on another classification, and permit the profit which he makes out of the marine insurance to carry his losses in the fire and casualty insurance. That, I say, is where the effect of your marine underwriters is at odds with the casualty.

BY MR. McKENZIE:

Q. Would you presume this situation, then. A marine underwriter does no other business. Would that situation concern your company in any way, with reference to taxation on that marine underwriting? A. In answering that question, I do not think it is a question before the Commission as to whether the tax on that marine underwriter would affect our company at all.

Q. It is merely a point you have raised in your submission? A. Definitely.

Q. I quite agree that it is not a point properly before the Commission. Thank you.

BY MR. ROBERTSON:

Q. Mr. McIntosh, Mr. Ham asked you as to your re-insurance policy, and I gathered by the tone of his voice that he thought he got you into trouble by your answer, that you insure with stock companies or that you associate with stock companies. Possibly you would tell the Commission why you associate with stock companies in your re-insurance? A. It is not my wish, gentlemen, to bring in any extraneous matter before the Commission. That is why I answered the question of Mr. Ham directly, that we do re-insure stock companies. As you know, in the fire insurance business the facilities of 168 companies operating in Canada are removed from the rest of the companies who are endeavouring to carry out their end of the insurance in this country. The re-insurance market is definitely limited; and in order to overcome the question of facilities which are offered to independent companies, our own company and a number of other companies have offered, to a limited degree, re-insurance facilities to companies who cannot find facilities for carrying on ordinary risks.

Q. Where does the limitation come in? Just tell us why there is a limitation, by which I take it you mean your company, Gore, is excluded from getting re-insurance from 168 companies? A. Oh, yes.

Q. How about that exclusion; is it enjoyed by other mutuals? A. Yes, the privilege is enjoyed.

Q. But the exclusion; is it enjoyed by other mutuals? A. Yes.

Q. And by other stock companies? Is the exclusion enjoyed by certain stock companies? A. I would say that the exclusion is enjoyed by certain stock companies of their own volition.

Q. And it is enjoyed by you, by the mutuals -- ?

A. Involuntarily.

Q. Just explain that?

BY THE CHAIRMAN:

Q. Is it enjoyed or suffered? A. Suffered is the word.

BY MR. ROBERTSON:

Q. That was what I meant by using the word "enjoyed".

A. The explanation of that is only that mutuals are not permitted to be associated in the Canadian Underwriters Association with the joint stock companies. I think for a short time, up to 1925, it was possible; and I believe the Waterloo Mutual at that time was a member of the Canadian Underwriters.

Q. But what happened to the Waterloo Mutual, in reference to the Canadian Underwriters Association? A. Their resignation from the association was requested.

Q. And that is one of the cash mutuals? A. Yes.

W. W. FOOT,

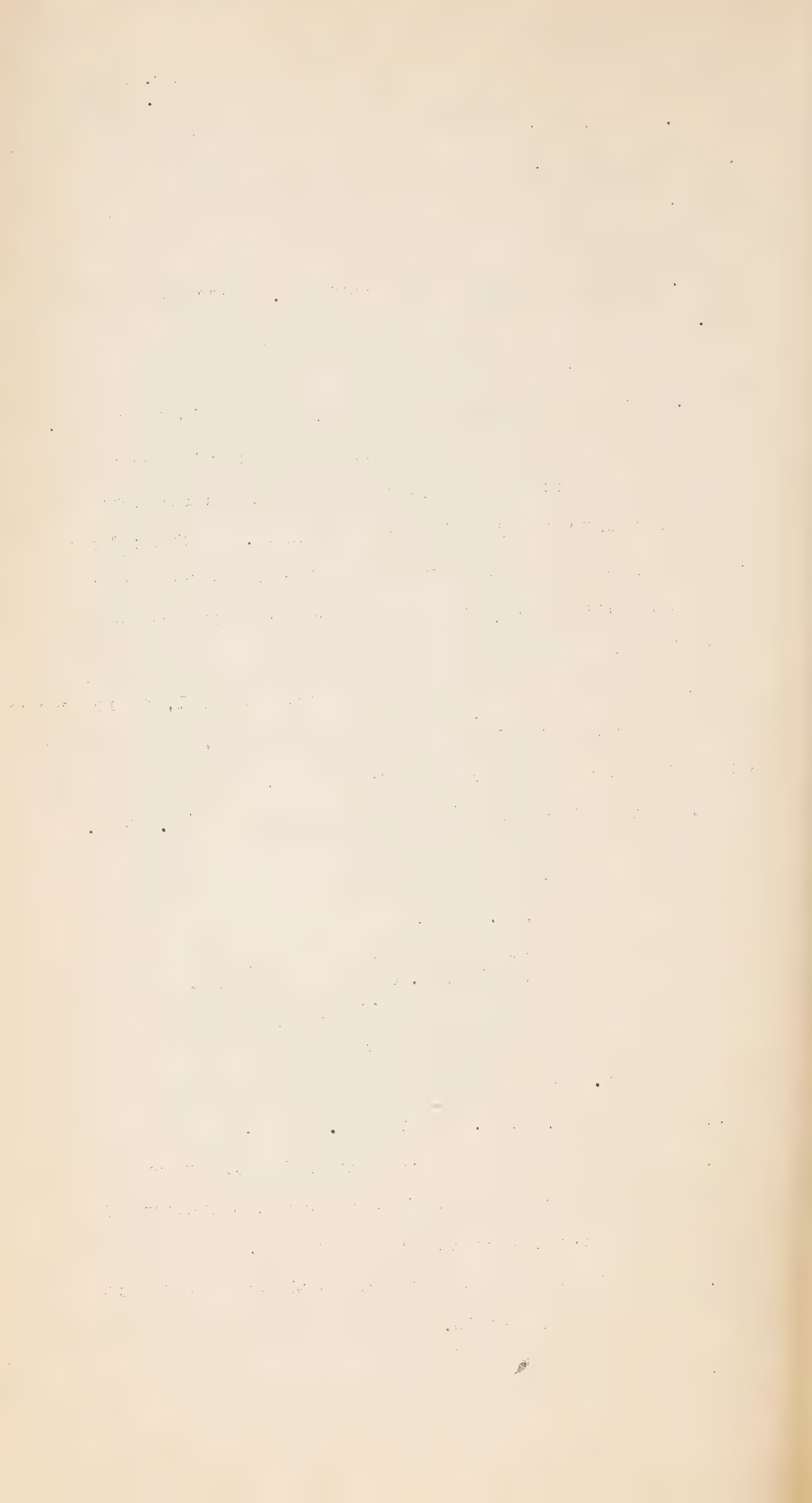
General Manager, Economical
Mutual Fire Insurance Company,
Kitchener, Ont.,
having been duly sworn,
testified as follows:

BY MR. ROBERTSON:

Q. You are Mr. W. W. Foot? A. I am.

Q. And what is your association in the insurance business? A. I am the general manager and secretary of the Economical Mutual Fire Insurance Company.

Q. Which is one of the parties on whose behalf this brief is filed? A. It is.



Q. Your head office is where? A. Kitchener, Ontario.

Q. And you have been in business since when? A. Since 1871.

Q. You are a cash mutual? A. We are a cash mutual.

Q. You have the premium note end of the business?

A. Yes.

THE CHAIRMAN: Does he do business exactly as Mr. McIntosh does? You may abbreviate his evidence a little, perhaps.

MR. ROBERTSON: Yes, I will.

Q. You do business just the same as Mr. McIntosh does, substantially? A. No.

Q. Just explain the differences. A. The Gore District participating business is predicated upon a dividend, whereas in the case of the Economical Mutual the dividend is given in the first instance at a rate 20 per cent below the non-participating policy holder. There is a note but not a dividend at the end of the note.

Q. Let me elaborate that in this way. There is no reason why you cannot pay a dividend? A. Oh, no.

Q. You can pay a dividend? A. Oh, yes.

Q. But in actual practice you have premium note policy holders? A. Yes.

Q. And non-premium note policy holders; that is, cash policy holders? A. Yes, sir.

Q. Your practice has been not to pay dividends? A. For about thirty years.

Q. Will you please explain how you give back to your premium note policy holders the advantage, if any, over the cash policy holders? A. We consider the non-participating premium in the first instance; and if the prospective

participating member qualifies as to suitability of the risk, I mean no undue hazards, and then if he is a morally good risk, by signing his premium note he becomes a member of the company and gets his rate of premium at 20 per cent below the non-participating policy holder.

Q. You have policies and applications? A. Oh, yes.

Q. You have re-insurance? A. Yes.

Q. You have office staff? A. That is right.

Q. You have agents? A. Yes.

Q. You pay commissions? A. Yes.

Q. And generally function, with the exception of the variations you have just mentioned, in a manner very closely similar to that of Mr. McIntosh's company? A. Yes; and in quite spirited competition with them.

Q. And in quite spirited competition with the stock companies? A. Oh, yes.

Q. They are quite spirited, and you are competitors?
A. Yes.

Q. How do you deal with the excess of receipts, or the deficiency, over disbursements in a year? Please explain, let us say, your underwriting gains and losses? A. The total excess of income over outgo from all sources has been for many years transferred to the general reserves of the company, for the protection of policy holders.

Q. What about your investment income; do you treat it --?
A. As part of the company's receipts; it is treated in that manner.

Q. What about your rates of premium and cost of insurance and commission paid to agents, in comparison with the stock companies? A. I think it is well to bear in mind that when the term "stock companies" is used, there are two

classes of them; those are the Canadian Underwriters Association, which are governed by the rules and regulations of that association, and there are other independent stock companies who have perfect freedom of judgment in rates and commissions and all matters relating to their business.

In answer to your question I would say that with regard to the stock companies in the Canadian Underwriters Association, our rates are lower than theirs in practically every instance; and the few exceptions that would apply would be classes of risks, particularly fire risks, where in our judgment the rate charged by them is insufficient. There are not so many of those. I think I would take say an unprotected flour mill, a chopping mill, as an example. Through recent reductions made by them, their rate level came below ours, as far as we could ascertain in competition, and we did not feel inclined to go below their rates, because of our judgment on that type of risk. With regard to the rates of the independent stock companies --

Q. What do you mean by "independent" companies?

A. Oh, there are many of them.

Q. What makes them independent? A. They are not members of the Canadian Underwriters Association. Through competition, and through judgment it can quite conceivably be that their rates in some instances are lower than ours; but I would say on dwellings, schools, churches and such classes as that, we are at least as low or lower, and in the mercantile business in many instances lower still.

BY MR. ELLIOTT:

Q. That refers to the cash plan? A. Yes, sir.

BY MR. ROBERTSON:

Q. Could you say, generally speaking, that on unprotected

risks your rates are lower than those of the stock companies?

A. By and large, yes.

Q. You spelled it out by farms and villages and mercantile risks and so on; but by and large you can classify it as unprotected property? A. Yes. Incidentally, Mr. Robertson, it should be borne in mind, too, that when this word "unprotected" is used in insurance terminology, that refers to a business without any protection whatsoever; that would be farms and the smallest of villages. Listening to the evidence here for the last few days, I think that when unprotected business is mentioned it should be borne in mind that there are semi-protected places, and places with varying degrees of protection that would not be similar at all to large cities with good fire departments, but that has been referred to casually, I think, as unprotected business.

Q. What portion of your business is in that kind of risk? I do not want the exact percentage, but is it large or small; is it infinitesimal or practically the whole of your business? A. In the case of the Economical I would think that we would write a smaller portion of unprotected business than the three other cash mutuals.

Q. What would you say from your experience and knowledge of cash mutuals, the other companies in addition to your own, about the volume of unprotected risk that they cover? A. I think the companies combined would write more of the so-called unprotected business than they do of the protected.

Q. What about their rates of commission? A. Our rates of commission, I think, in the smaller centres closely approximate the commissions paid by stock companies. In the larger centres, cities like Toronto, or Montreal, or Hamilton, or Windsor, or Ottawa, I think the commissions we pay in those

centres would be lower on the average than those of the joint stock companies.

Q. Do agents who act for you in any cases, or many cases, act also for the stock companies? A. Oh, yes, I think in the majority of cases; nearly all.

Q. I have here a circular letter which I received from you, sent out by the Ontario Insurance Agents' Association, or at least it is on their letterhead. Can you tell me where that came from?

MR. MANN: Could we have a look at that before you introduce it? It may be irrelevant.

MR. ROBERTSON: Certainly.

MR. MANN: Having seen the letter, I have no objection to it. I do not know anything about it.

THE WITNESS: That was given to me by an agent in Kitchener, and I gave it to Mr. Robertson.

BY MR. ROBERTSON:

Q. It has reference to this inquiry? A. Yes.

MR. ROBERTSON: Then I file that.

MR. MANN: That is a letter of the Agents' Association?

MR. ROBERTSON: Yes. It is headed, "Ontario Insurance Agents' Association," and purports to be signed by some official of the organization.

Q. I mentioned this morning, in the presentation, the competition in certain fields, at least I think I did and if I did not I wish to do it now. Do you have competition in the accident and sickness insurance which you write, from the life insurance companies? A. Yes. We transact group life and accident insurance in direct competition with the life companies transacting the same class.

Q. What is that? A. I said we are in direct

competition in accident and sickness insurance, particularly with regard to group insurance of that class, with the life insurance companies operating in Canada. In that connection it might be interesting to make the observation that in that class of business, which is a very finely priced class, we are assessed a premium tax of 3 per cent. Let us say we were in competition, as we frequently are, with the Metropolitan Life Insurance Company. That is a very large American mutual. On the same class of business in Canada they are taxed a premium tax of 2 per cent, and no income or excess profits tax to take up any slack. I think that is one case in point where there is an inequality in taxation against us that has not so far been mentioned in any of the briefs.

BY MR. PARKER:

Q. Mr. Foot, I am not quite clear in my own mind where you draw the line between an unprotected risk and a protected risk? A. In insurance terminology an unprotected risk is one with no protection whatsoever. In these hearings this week different witnesses have referred to unprotected risks, which I think certainly includes business that has been written in other places with varying degrees of protection.

Q. One witness may class a risk that is on the border line as a protected risk, whereas the next witness might call it an unprotected risk? A. There are five or six classes of protection.

Q. I am talking about protected and unprotected; I am not talking about degrees of protection. I am getting down to the point where they are unprotected entirely. Is that what it means? A. Unprotected business in the insurance terminology is business without any protection whatever.

Q. Let me see if I can put it this way. Take a small village, where there is a water system, and hydrants, and hose available to string to a fire in that village. One mile out or two miles out in the country, there is a farm risk, outside of the corporate body, which perhaps has no right to request aid from the village fire department. Where do you draw the line? I believe in a great many cases, however, the fire departments will go outside their area to help put out a fire, if they are invited to do so? A. Yes; arrangements are made in that way. But I do not think most companies look upon that as a protected risk.

Q. That is what I would like to get, some line of demarcation. When you make the statement that the majority of your business is of the unprotected class, there is all the difference in the world as to where you draw the line, is there not? A. Yes.

Q. Am I fair on this, Mr. Foot, that when a new policy is written in your company it can be either a participating policy or a non-participating policy, at the choice of the applicant? A. That is so.

Q. And if he chooses to become non-participating, he pays a cash premium of a certain amount? A. Yes.

Q. Which is ordinarily the same as that of a stock company in the same locality? A. Oh, no.

Q. What is the difference? A. In the case of the stock companies of the Canadian Underwriters Association, I would say that in nearly all cases it would be cheaper.

Q. The same risk and the same hazard? A. Yes. In nearly all cases it would be cheaper.

Q. What do you base that on? Why do you say that? I understood from the last witness that in his company the

non-participating premium was practically the same? A. It is often practically the same as the joint stock companies who are not members of the Canadian Underwriters Association.

Q. Perhaps that is what he said; I may have misunderstood him. A. I think it was something along that line.

Q. That is what you say, in any event? A. Yes.

Q. Then what is the difference between the stock company premium, that is the company who is a member of the Canadian Underwriters Association, and that of the rebel or non-tariff member? A. That might run anywhere from 5 to 50 per cent, depending upon their judgment.

Q. Each fellow goes on his own? A. Yes.

Q. He can under-cut and underwrite as much as he likes? A. Yes.

Q. That is the way it works? A. Yes.

Q. Then if he decides to become a participating member, which you say is purely a matter of choice on the part of the assured, he pays a cash payment of 20 per cent less than the other one; or does he give a premium for an amount 20 per cent less? A. He gives a premium note.

Q. He does not make any cash payment in advance?

A. Yes, he does.

Q. What does he do? He puts down how much cash?

A. Could we take a case?

Q. May I take it in this way. We will say it is a premium for a period of three years. A man comes in and says, "I want to pay my premium and be done with it." Let us say the premium is 80 cents per \$100 for three years, so the premium will be \$80? A. Say the premium is \$25; it will be easier to compute. The cash premium in that case would be treated in this way under the mutual system, and

this is in the Economical Mutual Fire Insurance Company. He signs a premium note for \$100 payable --

Q. For \$100? A. Yes, four times.

Q. A demand note? A. No. That is set out in the Ontario act. It is a statutory form.

Q. Just tell me; is it a demand note or a time note?
A. It is a time note.

Q. Three years? A. Yes. Payable in cash on the first day, \$20.

Q. What is the first day? A. That is the date of the policy. In the second year another \$20 is payable; in the third year a third \$20 is payable. Then if at the end of the three-year term there is no demand made upon him, his note is returned to him. The unearned portion of the note would amount to \$40.

Q. If no further assessment is required he is returned the \$40? A. The residue of the note, amounting to \$40.

Q. The balance of the note is cancelled and the note is surrendered? A. Yes.

Q. And you have collected \$60? A. Yes.

Q. Whereas from the other man who took a three-year policy straight, you would have collected how much? A. I thought you meant that this was an annual proposition. He would have paid \$75 against \$60.

Q. No; I took the three-year term. A. I see the difficulty there. Mutual business is all three years.

Q. That is what I thought; and there is a good deal of stock business on the three-year basis? A. Yes.

Q. Then let us start again. Take it my way this time; perhaps I can understand it better. A man comes in, and he has his choice of paying a three-year premium. I suggested

an amount of \$80, but you said it would work out better if you took an amount of \$25. A. Take the \$80.

Q. Will that work out just as well? A. Yes.

Q. That is his three-year premium? A. Yes.

Q. The other man says, "I do not want a non-participating policy; I want a participating policy." What does he do?

It is the same hazard, the same risk. A. He gives a premium note for \$320.

Q. A three-year note? A. Yes.

Q. He pays how much immediately in cash? A. No, I am wrong. He gives a note for \$106.65.

Q. Payable in three years? A. Yes.

Q. Without interest, or with interest? A. Without interest.

Q. He immediately pays an amount of how much? A. \$21.33.

Q. And at the beginning of the second year he would pay another \$21.33? A. Yes.

Q. And the same for the third year? A. Yes.

Q. That is a total of \$63.99. If everything has gone along in normal fashion, with an average number of losses and all that sort of thing, his note will be surrendered at the end of the term? A. That is right.

Q. And he will have paid \$63.99, while the other man would have paid \$80? A. Yes.

Q. What else does this man get? Does he get some of that repaid to him later on by way of a dividend, some of that \$63.99? A. He has not, for the last thirty years. No.

Q. Previous to that he did? A. Previous to that he did.

Q. What has become, during the last thirty years, of those amounts which up to that time were being paid back to

these policy holders? What has been done with them? A. They are held in the general reserve of the company.

Q. The general reserve has been going up and up?

A. That is right.

Q. Until it is now very substantial, I suppose? A. Yes.

Q. Is there any limit to it, as to what you can build that up into? A. That would be a matter of company policy, I think.

Q. They have not reached the saturation point yet, in any case? A. I do not think they have.

Q. What amount do they have in proportion to the amount of insurance carried? Can you tell me that approximately? What is the amount of their general reserve in comparison with the insurance carried? Perhaps it is in the table. Are those the figures on page 8? A. Yes. The general reserve is \$2,940,246.

Q. Is there any objective set by the company, as to what that shall be built up to before you will start repaying something to the participating members? A. The formula on which that has been built up through the years is the permissive one outlined on the previous page of the Ontario Insurance Act.

Q. That is, your policy is to go along with that?

A. That is right.

Q. The accountant points out to me that from the statement your surplus is between a half and three-quarters of a million dollars now in excess of the maximum required by the act. Is that correct? A. Oh, yes. That does not take into account liabilities that the company might be faced with in respect to automobile and the majority of casualty lines. In the case of the Economical we have a liability in western Ontario, in five adjoining counties there, under windstorm

insurance on farm property, and this windstorm hazard is not to be confused with the type of windstorm that is included in the so-called supplementary contract of fire insurance which is applicable to town and city properties.

I guess I am not disclosing any company secrets when I say that hazard is one that has given us some consideration. There is no use calling out the fire brigade if a windstorm, of very severe proportions, confronts you. We have tried to study the meteorological data of that area with regard to the prevalence of windstorms there. Last year a very heavy one hit the county of Middlesex, and we are in doubt to some extent as to the probable losses we may face in that class in that relatively small area. I have not the figures as to the liability for 1944, but at the end of 1943 under windstorm it was \$3,500,000. Premiums have gone up very substantially in one year, due to the withdrawal of certain companies from writing that class. This is only one case, but I would say that our liabilities, at a guess, in that area must be approaching \$5,000,000 at the present time.

Q. I wonder what all that adds up to? You still have this reserve of up to three-quarters of a million dollars in excess of the statutory requirements? A. In excess of the statutory requirements with regard to fire insurance only, but not with respect to other classes.

Q. But you are taking off the man who is carrying fire insurance; you are building up some of his money into a reserve to help you carry on automobile and windstorm and the other casualty hazards? A. I suppose that is true.

Q. Just one other thing. Perhaps this is not very much to the point, but in the case of a great catastrophe, a great conflagration, when you would be hard hit, your reserves are

the only thing you have to draw upon? A. That is right; and the premium notes.

Q. That is, those that have not yet been cancelled; the ones outstanding? A. Yes.

Q. And the participating policy holder has his liability limited to the extent of that note? A. That is right.

Q. In other words he is in exactly the same position as the man who has bought shares in a company, to take your figures, amounting to \$106.55, but who has paid up only \$63.99. On winding up or insolvency, he is called upon to pay up the balance of his stock, to help meet the liabilities of the company. That is the way that works, and that is the way this participating policy holder would work. Right?

A. I would like to answer that question right away --

Q. Then what is the real difference between the two of them, in essence? I do not care what label you put on it, but in substance what is the difference? A. I would be glad to make a later statement on that, if it were possible to do so, after I have given it some thought.

Q. At the moment you cannot see any difference?

A. It is an analogy that I have not studied.

MR. ROBERTSON: Are you not asking him, Mr. Parker, really to answer what in essence becomes a legal proposition? You are asking a layman to interpret the significance of the winding up of a company, and all the things that go into the liquidator's proceedings. I think you are.

MR. PARKER: You think that is a question of law?

MR. ROBERTSON: I think it is a question of law. I have not any serious objection to the witness answering it, but he says he wants to think about it.

THE CHAIRMAN: I think he is entitled to do that.

MR. ROBERTSON: Do not misunderstand me; I have no objection to his answering it, but the witness says here is something he does not just understand what he is getting into, and he would like to think about it.

MR. PARKER: The record will show what he says, and I will not press it beyond this.

Q. The expression was used recently in comparing one with the other that the mutual company was assimilated to an ordinary company. Would that convey anything to you?

A. I have heard that.

Q. Does it mean anything to you, as an insurance man?

A. I think there is a great deal of similarity in operation in classes of business written and contracts, and so on.

Q. And a great deal of similarity in respect of the limited liability of the participating policy holder, and a great similarity between his position and that of a shareholder who has subscribed for more capital than he has fully paid up?

A. With regard to his liability, yes. With regard to the service he gets and the protection he gets, perhaps no.

Q. That may be quite true. I think the last witness said that in his opinion about 10 per cent of their total insurance was participating and 90 per cent was non-participating; can you tell us what your fraction would be? A. I cannot give it offhand.

Q. Not to the dollar, but roughly? A. I cannot give the premium or risk figures. I can get it, but ---

Q. Would it be three to one, or fifty to one? A. We have about 2,000 participating policy holders.

Q. I do not care about that; what about the dollar value of insurance? A. I have not got that figure, but I can get it.

Q. Can you not tell me whether it is roughly 2 and 1 or 3 and 1 or 4 and 1 or 10 and 1? A. I would say it is certainly more than 3 or 4 and 1.

Q. Just give us your approximation; that is all I want. A. I would guess about 10 and 1.

Q. About the same as the other one was. A. About that.

Q. And from your knowledge the other two in the group would be about the same? A. Yes, approximately the same.

Q. You referred to the qualifications required to become a participating policy holder. What are the qualifications? What must a man be before you will take him as a participating policy holder? A. What I would call a standard risk.

Q. It does not depend upon his politics or his religion, I take it? A. No, nothing like that.

Q. Then, upon what does it depend? A. I might say that I am sure we would be only too glad to have anybody in this room as a participating policy holder.

Q. I am sure you would. In the main, what is the meaning of that qualification? A. The risk must stand inspection, the ordinary normal standard of inspection. That is to say, if there are glaring hazards in it, and those cannot be corrected, we will not accept the risk. For that matter, we would not accept it on either plan.

Q. That is just the point I am coming to.

A. And if a man has a good moral reputation.

Q. If he has a bad fire record you do not want him under either class? A. Correct.

Q. I want to know what he can do to get in as a non-participating policy holder if he is not good enough to come in under the other class? A. He has complete choice. There is one standard policy; Mr. Robertson has a copy of it, I believe.

Q. I have heard you use the word "qualification". I am now asking you if you make a distinction between the qualifications of a participating holder and a non-participating holder? A. No, none at all.

Q. You do not make any distinction. A. No, not at all.

Q. You have also said that all the questions I asked Mr. McIntosh about the employment of agents, and agents acting for both mutual and joint stock companies -- the same agents represent both? A. Yes, the same type of agent.

Q. Has your company, ever since its organization, been writing both types of policy, or has it been limited to the premium note? A. It started off on the premium note plan only.

Q. Only? A. Yes. Then, seven or eight years later ---

Q. About 1871, did you say? A. Yes; then, close to 1880 the company was confronted with a very heavy assessment on its members, due to the fire experience at that time, and took advantage of the permissive section of the Ontario Act to transact business on the cash plan as well.

Q. It was not a case of compulsion? A. No.

Q. It was purely a matter of choice? A. Yes. They went on for some years and for the further advantage of the mutual policy holders, participating policy holders, they paid a dividend, in addition to the reduction which they got in the manner you have just described. That continued until 1903, the year of the Toronto fire, when the company was practically wiped out. It had only \$30,000 of cash and assets left. From that time on the dividend policy was restricted, and reduced from the former figure, until it became so small that the mechanics of returning the dividend to the mutual policy holders outweighed much of the advantage that the company got out of it. The directors at that time concluded that it would be better to give the lower rate in the first instance, and that policy has been pursued. I believe it might have been changed some years ago, except for the entry into the field of the dividend paying mutuals from the United States. In competition with them there were many instances where we were asked to protect business we already had written and held, and to quote a net rate as against them which would be the equivalent of their gross rate, less the dividend. And in the opinion of the company, in later years it was felt that they could not continue to pay at 30 per cent, as performed by those companies; and they have since continued to try to give the mutual policy holders a low rate in

the first instance. How long that will continue is not for me to say.

Q. Can we sum it up in this way, that your experience at the time of the fire led the company to believe that it was not a safe and practical method of carrying on business, and you had to adopt some other method of keeping the reserve up to what would be safe; is that fair? A. Yes, in a general way that is correct.

Q. You never paid any income tax in recent years? A. No.

Q. You have never been assessed? A. No, never assessed.

Q. Did you ever make a return? A. Yes.

Q. Have you made returns right up to date? A. Every year a nil return.

Q. You go through the motions, so to speak, and file a return, simply to report any income; and that has been the end of it. A. Yes.

Q. Do you do foreign business, as well? A. No, none.

Q. Do you know about the other two? A. The Waterloo and Perth do no foreign business whatsoever.

Q. You pay the premium tax. A. Three per cent.

Q. On what do you pay 3 per cent? A. We pay 3 per cent on the premiums written in a year.

Q. Let us get that carefully. To begin with, I take it it is 3 per cent on what we will call non-participating premiums? A. No, on all premiums.

Q. Take them one at a time. Let us take first the non-participating, and as an example we will refer to the one mentioned a minute ago, where the man pays \$80. I understand he pays 3 per cent on the \$80? A. Yes, he

pays 3 per cent of \$80.

Q. On what portion of the premium note do you pay the 3 per cent? A. What was the instalment?

Q. It was \$21.33. A. We would pay 3 per cent on \$21.33 each year.

Q. When a man pays \$80 three years in advance, you pay it all in the year in which it is written? A. Yes, all in the year it is written.

Q. And, in addition to those two items, you pay 3 per cent on what else? A. On all classes of business written by the company.

Q. That takes in all classes of business? A. Yes, fire, casualty, automobile and everything else.

Q. Do you pay 3 per cent on your investment income? A. No.

Q. You do not pay anything on that? A. No.

Q. That was raised within the last couple of years, was it not? A. The premium tax, do you mean?

Q. Yes. A. It stayed with us the same as it had been before. We paid 2 per cent to the provinces in the case of ---

Q. I was coming to that; prior to the Dominion-Provincial agreement you were paying 1 per cent on those same items? A. To the Dominion Government.

Q. And 2 per cent calculated in the same way. A. Yes.

Q. To the Provincial Government. A. Yes, to the various provinces.

Q. In which you do business. A. Yes.

MR. MANN: It worked out at a small fraction more than that.

BY MR. PARKER:

Q. For all practical purposes, it was 2 per cent, on the average? A. Yes.

Q. And, under the provisions of the agreement the provinces surrendered that, and the federal tax was placed at a straight 3 per cent. A. That is correct; we still, of course, pay the fire marshal tax to the provinces.

Q. I am talking only about the premium tax. Do you know whether that applies in the same way to the other four companies? A. I think so.

Q. What you have said as to the basis of calculation of the rate applies to all four cash mutuals? A. I do not know about the Gore. Mr. McIntosh could answer that for himself.

BY MR. ROBERTSON:

Q. There is one question I think I should clear up at this time, just to keep the record straight. In answering Mr. Parker you made certain statements with respect to similarity. To put it as he put it, he asked about the similarity between stock companies and your company. There was some discussion as to the similarity of operation, and then he went into the other field of stockholders and policy holders. Would you please tell the Commission how far you can go in connection with that matter of similarities? What are they? A. Well, there is a similarity in the method of acquiring the business. There is some similarity with regard to the underwriting, although many companies have rates and rules provided to them by their organizations, whereas we have to provide our own. There would be similarity in the method of accounting, and in the method of reimbursing the agents by way of commission. I do not say

this in any critical way of any other insurer, but similarity in settlement of losses exists. Until we lost so much of our staff on account of the war we tried so far as possible to settle our losses by means of our own company adjustors. That would not apply, of course, if we were writing a risk in Vancouver, because we have not got a man out there. But wherever the loss can be reached, either from the branch office or the head office, we have made every attempt to settle our losses through adjustments made by our own men. There is this to remember, that I am not the company. I merely work for the company, and carry out the provisions and directions issued by the board of directors. Does that answer your question?

BY MR. PARKER:

Q. Your managerial duties are much the same as those of the manager of a joint stock company? A. I think they are much more difficult, sir.

BY MR. HAM:

Q. You made the statement, one which is absolutely correct, that the commission rates closely approximated those of the joint stock companies in rural areas, and were lower in the bigger centres; is that correct?

A. Yes.

Q. May I direct your attention to the blue book which shows the commissions right across Canada for your company as 26.38? A. In what class of business is that?

Q. Fire. A. In all Canada?

Q. And it shows the average for all Canadian companies, including your own, as 24.85. You are No.22 in the column. A. Yes, the figures are 24.85 and 26.38.

I can understand that.

Q. Then, would you explain it? Can you reconcile it?

A. Yes. The average of all companies operating is brought down by many companies which would pay a very much lower commission on renewal business than would be paid by the stock companies in operation, where they pay practically the same commission every year.

Q. Can you suggest the name of any company on the list which would operate on that basis? A. Yes, I think there are some and then, again, those figures are the result of applying the net commissions paid in the companies' ledgers as against the premiums written for that class in the same year. And through the operations of a company all re-insurance commission and all other adjustments on commissions flow to produce the final figure.

Q. That affects one company, by and large, as it affects another? A. I do not know how it affects the other, but I have had that point raised before; and, regardless of what figure is there, I would still say that in the larger cities we pay less commission on the average than the board companies. And in the rural areas and smaller cities we pay pretty much the same.

Q. Do you write through general agencies in any province? A. We used to, and that would tend to put our figures up.

Q. Did you for 1942? A. In 1942 in the province of Quebec we did substantial business through a general agency, which was discontinued as of the first of this year.

Q. I might pursue the inquiry in respect to the independent fire insurance conference and the independent automobile conference. The Economical belongs to both

those conferences? A. Yes, we belong to both.

Q. And does it happen that you hold an executive office in either or in both? A. Yes, I am chairman for Ontario for the fire conference.

Q. Taking first the independent fire insurance conference, has it considered or put into practice the control of rates among its members? A. No, no control.

Q. They do not discuss rates at all? A. They have discussed rates, yes. They have tried to collate information which would bring about certain information with respect to what was being done in independent companies with regard to rates. That information is now in process of being compiled; it is not complete, and I have not seen it yet. But it arose from the fact that frequently one independent company would be found writing at rates which upset the construction of rates as used by practically every other company. And it is a question as to whether that one company was right or whether the others were right. We have no organization such as you have to keep track of the experience of our members, and we are subject to no such control.

Q. You appreciate that I do not deprecate that objective at all? A. No, I understand that.

Q. Has the conference considered the promulgating of uniform forms? A. Yes.

Q. And what about the automobile conference; what about the agreement on rates there? A. I am not on the executive of the automobile conference, but one of our officials is, and I have discussed the matter frequently with him. That conference has considered the question of automobile rates in the last number of years, and the members of the conference meet and

consider the rates and the experience in automobile insurance reported by all companies.

BY THE CHAIRMAN:

Q. You mean the Canadian underwriters? A. Yes.

MR. PARKER: Probably he means that they consider them too high.

THE WITNESS: They consider those rates. It should be borne in mind, in connection with automobile insurance, that every company is required to report its statistics and every branch of its business to the reporting bureau, which is set up with the government's blessing. Those figures are available to everyone who writes automobile business, and they are available to anyone who wishes to see them. The automobile conference considers the experience of automobile insurance in all the different provinces by class of risk, and by form -- P.L., P.D., fire and theft, and they see if it is possible to reach any form or any plan of uniformity with regard to rates over a given period. If, in our judgment, we think that the suggested rate level of the conference is fair for that risk, we have a perfect right to subscribe to it. And if we do not agree with their decisions, or if we do not think that the decision of the majority of the conference is correct, we do not abide by the rates adopted by them.

BY MR. HAM:

Q. You would not suggest that in carrying out that plan there was anything monopolistic in it, would you?

A. What does monopolistic mean?

Q. Well, I am quoting from your brief. Would you consider that in carrying out the plan as set out in the automobile conference there would be anything

monopolistic in it? A. With my own conception of the meaning of the word "monopolistic" I would say that there is nothing monopolistic about it at all. It is just an exchange of information to see what adequate rate can be set, in the interests of the public, and in the interests of cost of acquisition and of rate making. If it were a monopoly, then I could not withdraw from any arrangement, but with regard to my given word to abide by the rates agreed upon for the present year, I can withdraw tomorrow, if I choose to do so. So I do not think it is monopolistic, as I would understand that word.

MR. PARKER: My learned friend suggests it should be a study group, possibly.

BY MR. HAM:

Q. Can you help me in your capacity as an officer of the independent fire insurance conference, and tell me if any or all of the American Mutual Alliance members are members? Are all or some of them members?

A. Some are.

Q. You do not know whether all of them are, but you do know that some are? A. Yes, some are.

Q. Some of them are members of that conference?

A. Yes.

BY MR. ELLIOTT:

Q. In the past few years has your company departed much from the suggested rates of the conference, in either field? A. There are no suggested rates in fire. In respect of automobile, I think the suggested rates have been in force -- and if I am wrong I should like to be corrected -- for four or five years. The automobile conference has probably been in existence for about seven years. Prior to that time there was no attempt

to study rates other than in a casual way. Automobile insurance is one of the most difficult businesses to be found, and yet at the same time it is one of the simplest, because the form used by every company writing that class of insurance is identical. It is a statutory form. Consequently, it can be determined quite accurately whether, on the average, the companies are charging too much or too little for the various classes of risk.

BY THE CHAIRMAN:

Q. Your company has not disagreed, to any substantial extent, with the independent automobile conference?

A. Our judgment was that it was a pretty fair level, and that level would be, on an average, perhaps 8 or 9 per cent below the rates charged by the Canadian Underwriters Association company.

BY MR. ELLIOTT:

Q. Does your company retain the right to cancel a contract of insurance? A. Oh, yes.

Q. That is true of all contracts written on the cash plan, as well as the participating plan policies?

A. It certainly is true of the business written on the non-participating plan. But I do not think I have ever had that point raised with regard to the other plan.

MR. MANN: It is statutory, I believe.

THE WITNESS: I think that is right, yes.

BY MR. ELLIOTT:

Q. The policy will be the same in that respect.

A. Yes, I think so, but I have not had that point raised before.

Q. So that you have not, in fact, in your experience terminated a policy with a contract holder on the participating plan? A. I cannot remember an instance

where it was done at the request of the company. It happened frequently at the request of the insured.

Q. And when that happens, at the request of the insured, on the participating plan, what is the result?

A. That would be at the standard short rate -- short date rate.

Q. He makes that payment on his note, and then gets back his note? A. Yes.

Q. And that is the end of it? A. Yes.

BY MR. McKENZIE:

Q. I understand your company does not write marine insurance? A. Not ocean marine.

Q. Or any other marine? A. It writes inland marine.

Q. What inland marine is that? A. Inland marine is commonly dealt with in the various branches of the business.

Q. Do you mean water borne cargo? A. No, not water borne cargo.

Q. Not cargo anywhere by water? A. Truck transit and personal property insurance.

Q. P.P.S.? A. Yes.

BY MR. MANN:

Q. You call that inland marine? A. Yes, that is called inland marine insurance.

BY MR. McKENZIE:

Q. You mean land insurance. A. No, that is a definite class of insurance.

MR. McKENZIE: The position of the Canadian Board of Marine Underwriters is set out in our brief as follows:

"To the Honourable, the Chairman, and Members of the
Royal Commission on Co-operatives:

Statement of Submission on behalf of The Canadian
Board of Marine Underwriters

"The Canadian Board of Marine Underwriters is an association representing all marine underwriting companies operating in Canada. One of the functions of the board is to act on behalf of marine underwriters in matters involving them in any proposed taxation legislation.

"It has been brought to the attention of this board that a representation has been made to this Commission recommending the imposition of a tax on marine premiums by way of an amendment to the Special War Revenue Act. This representation has been made by mutual insurance companies who do no marine business and who are in no way in competition with marine underwriters.

"The Canadian Board of Marine Underwriters opposes any such recommendation and submits that the scope of the reference to the Commission under P.C. 8725 is limited to 'a full public inquiry into the application of income and profits tax measures' under the Income War Tax Act and the Excess Profits Act.

"Furthermore the reference does not contemplate any inquiry into the application or amendment of the Special War Revenue Act which is clearly and admittedly neither an income or profits tax measure.

"It is therefore respectfully submitted that any recommendation of taxation on marine premiums by way of an amendment to the Special War Revenue Act is contrary to long established government taxation policy and is not a proper subject of inquiry or recommendation coming

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Mr. Foot

within the scope of the reference. It is consequently a matter with which this Commission is not concerned nor upon which it is empowered to act."

THE CHAIRMAN: I understand that that disposes of this case?

MR. ROBERTSON: Yes.

MR. PARKER: Perhaps this would be the appropriate place to discuss another matter. Last night, and again this morning, I spoke to some of the counsel with a view to determining just how we might close this section of the inquiry.

MR. GRAY: Perhaps before Mr. Parker makes his statement I might ask the privilege of saying just a word with respect to some material I have here.

THE CHAIRMAN: Very well.

MR. GRAY: When Mr. Gruhn was here I asked leave to file a supplementary statement given by him to the Congressional inquiry at Washington in 1942, with reference to a particular matter. The Commission was good enough to say that I might do so at a later time. I have it with me today, and I intend to file a photostatic copy of it, but would like to read it into the record first. Perhaps I might read only a few paragraphs from one page.

THE CHAIRMAN: It is not necessary to read it now.

MR. GRAY: Very well.

THE CHAIRMAN: I suggest that we take it as read and have it transcribed in the record.

MR. GRAY: That would not be entirely satisfactory, but if the Commission wishes to do it that way I am satisfied to have it done.

THE CHAIRMAN: We are thinking of the time element.

MR. GRAY: If it becomes necessary to refer to it at some future time I might have the privilege of reading it then.

The copy I have here, and which I shall hand to the Registrar is as follows:

"The Factory Mutual companies do not have access to figures for other mutual companies and, accordingly, are not in a position to furnish all of the data requested. However, so far as the companies of the Associated Factory Mutual group are concerned, we have prepared in the short time available a statement, partly estimated, that furnishes you the information requested. Such a statement follows:

<u>Year</u>	<u>Insurance in force</u>	<u>Premium deposits in force Dec. 31¹</u>	<u>Losses incurred¹</u>	<u>Gain or loss from operations</u>
1932	\$ 8,298,677,401	\$ 46,813,570	\$ 1,451,126	511,046
1933	7,835,292,619	43,809,817	1,615,954	762,693 ²
1934	8,094,181,627	44,965,004	1,532,627	519,878 ²
1935	8,328,670,382	45,893,232	1,515,908	168,187
1936	8,828,265,405	48,106,963	3,077,230	635,664
1937	9,431,614,548	50,847,258	2,369,614	54,384
1938	9,673,619,773	51,651,391	5,326,525	4,157,195 ²
1939	10,021,108,021	53,053,005	2,009,634	206,821
1940	10,500,306,940	55,576,257	3,115,439	384,586 ²
1941	<u>12,684,729,244</u>	<u>65,259,850</u>	<u>3,951,957</u>	<u>30,917²</u>
Total ten years			25,966,014 ²	4,279,167

¹Figures from Best Insurance Reports.

²Represents deficit

"It will be observed that in five of the past ten years, the operating results were such as to permit additions to surplus. In the remaining five of the ten years, the reverse was true and surplus was drawn upon. The net result for the ten-year period was to decrease surplus by \$4,279,167 on account of operating losses.

"This result is obtained after adding or subtracting from the underwriting gain or loss of the companies the profit or loss on securities actually disposed of in each of the ten years.

"The deficit in operating earnings in the ten-year period was almost entirely due to the very severe losses suffered by the factory mutual companies at the time of the New England hurricane in September 1938. These losses were several times the normal expectancy. Fortunately, the companies had accumulated what amount to conflagration reserves to take care of unusual losses when and as they occur and thus prevent undue fluctuations in the percentage of the original deposit that is returned to our members.

"Obviously, it is of advantage to business organizations to have a fairly stable insurance cost rather than a cost that might fluctuate widely from year to year. This conflagration reserve was accumulated by the factory mutuals over a long period of years to iron out fluctuations in the rate of return of unabsorbed deposit and thus meet the wishes of businessmen for a relatively stable cost of insurance.

"In years of favourable experience, a very small charge is made against each outstanding policy for a contribution to this reserve fund. Then, in years of abnormal loss experience, the fund is drawn upon as was done

in 1938 and also, incidentally, was done at the time of a serious windstorm in the south in the fall of 1936.

"While the operations of the factory mutual companies during the past ten years have shown an operating deficit, it is likewise true that the assets of the companies over claimable reserves have increased. The market value of their assets, as shown by the statements filed with the insurance departments of the several states in which these companies are licensed, exceeded claimable reserves at the end of 1932 by \$3,462,000; whereas, the excess at the end of 1941 was \$10,561,000. This increase in assets resulted entirely from the general rise in the market values of the securities held in the investment portfolios of the companies and not from their operations.

"It follows then, that the increase in what is termed surplus, that is, the excess of value of assets over claimable reserves during the particular period under review, was entirely the result of appreciation in market value of securities. This increase in surplus is purely a bookkeeping item and is subject to the rise or fall in security prices generally. It does not represent realized profits.

,"The Associated Factory Mutuals insure large individual risks. The average risk at the present time is in excess of \$1,000,000. While their normal losses are small, the companies are subject to total destruction of individual risks from time to time and for this reason require the maintenance of reserves sufficient to take up the shock of such occasional heavy losses. As the experience in the 1938 hurricane proves, reserves for unusually large individual or aggregate losses are

a necessity for the maintenance of the financial stability of insurance organizations.

"Representative Dingell raised a question with regard to the 'loading' if any, which is included in the deposit that the companies require their members to make. In response to this question, we replied that there was no 'loading', and there is none. The size of the deposit required of factory mutual members is determined at an amount that the management of the companies believes will be adequate to take care of all liabilities, including extraordinary losses, and also provide sufficient reserves to maintain the financial stability of the companies. If, however, the deposit proves to be insufficient, then each of the companies has the right to assess its policy holders for additional amounts up to five times the original deposit.

"The deposits required of the members or policy holders are not premiums but represent a fund from which the premiums, that is, the cost of insurance, is taken, and the balance, after allocating a very small amount to conflagration reserves, is returned to the member as a so-called dividend, which in reality is not a dividend at all but nothing more or less than the return of the unused portion of his original deposit. At the present time the average deposit per \$100 of insurance is roughly ten times the current annual cost of carrying the insurance. In other words, 91 per cent of the original deposit is currently returned as unabsorbed deposit on policies that have been in force for one year.

"The reason for requiring a deposit so much greater than the anticipated annual cost of carrying the insur-

ance is that the risks are individually large (averaging over \$1,000,000 at the present time) and the coverage provided by the companies includes the perils of wind, sprinkler leakage, limited explosion, falling aircraft, etc., in addition to fire insurance. The wind hazard is particularly subject to wide fluctuations from year to year. The hurricane experience in 1938 is one example and there are others, including a wind loss in 1936 on a single factory which amounted to more than \$1,000,000. Of course, the losses from the other hazards are also subject to variation so that for an individual year it is not possible to even closely estimate the amount of the deposit that will be required to pay losses.

"This low cost of factory mutual insurance is made possible by the large amount of time and money that is devoted to real fire-protection engineering. Every risk is visited regularly by trained fire-prevention engineers of wide experience and complete reports and recommendations are submitted to the companies and to the assured and where the United States government is involved on war work, its representatives also receive data from these inspections. This inspection service has earned a reputation for thoroughness and ability that is, in our opinion, superior to any in the field of insurance and we are confident that our efforts continually result in the conservation of the national wealth through the prevention of loss from fire, explosion and other hazards. In many cases our members consider that our fire prevention engineering service alone is worth all that they pay for their insurance.

"We trust that the above information fully meets

the request you made of us at the hearing April 9, but if not, we are at your service and will gladly supply any further information regarding our factory mutual companies.

"The factory mutual companies are desirous to place full and complete information before your committee, as we are confident that with an understanding of the methods of these companies, you will decide that we are entirely justified in our claim that, as purely mutual companies operating without purpose of profit, we are entitled to a continuance of the exemption from income taxes that has been granted by the Congress for many years.

Very truly yours,

Hovey T. Freeman,

President, Manufacturers Mutual
Fire Insurance Company, and
Chairman, Legal Committee, The
Associated Factory Mutual Fire
Insurance Companies."

Then, I place on record this letter from the office of the Commissioner of Internal Revenue at Washington, addressed to the Manufacturers Mutual Fire Insurance Company at Providence, Rhode Island. It states:

"Reference is made to the evidence submitted in support of your claim for reconsideration of bureau ruling dated April 1, 1931, holding that you are not exempt from federal income tax.

"The evidence presented discloses that your company was incorporated in 1835 under the laws of the state of Rhode Island. In an affidavit submitted it is stated that your company is one of the associated factory mutual group of fire insurance companies commonly referred to as factory mutuals; that all members of the factory mutual group confine themselves almost entirely

to the insurance of industrial plants located throughout the United States and Canada; that the object of the group is, first, the prevention of loss and its interruption to business and, second, to provide its members with insurance at cost against the hazards assumed; that your organization is purely a mutual insurance company whose only members are policy holders; that your income is derived from premium deposits and miscellaneous receipts and is used to pay losses and expenses or returned to your policy holders; that you do not have capital stock; that none of your income inures to the benefit of any private shareholder or individual; that your organization is without profit and is owned and controlled by your policy holders; that all policies are written on a participating basis and are subject to an assessment which is limited to five times the amount of the premium; and that each policy holder is a member of your company and is entitled to vote at your meetings.

"Based on the facts presented, it is held that you are entitled to exemption under the provisions of section 101 (11) of the Revenue Act of 1934 and the corresponding sections of the Revenue Acts of 1932, 1928 and 1926. You are not, therefore, required to file returns for the years covered by these Acts. Inasmuch as section 101 (11) of the Revenue Act of 1936 is similar to section 101 (11) of the Revenue Act of 1934, returns will not be required for subsequent years so long as there is no change in your organization, your purposes or method of operation.

"Bureau ruling referred to above holding otherwise is modified accordingly.

"Any changes in the form of organization or method

Mr. Gray

of operation as shown by the evidence submitted, must be immediately reported to the Collector of Internal Revenue for your district in order that the effect of such changes upon your present exempt status may be determined.

"The exemption referred to in this letter does not apply to taxes levied under other titles or provisions of the respective Revenue Acts except insofar as exemption is granted expressly under those provisions to organizations enumerated in section 101 of the Revenue Act of 1936 and the corresponding sections of prior Revenue Acts.

"A copy of this ruling is being transmitted to the Collector of Internal Revenue for your district.

"By direction of the Commissioner.

"Respectfully,

Sgd. Deputy Commissioner."

Then, I place on record too, a telegram dated April 18, 1945, from Mr. R. H. Lord to myself, as follows:

"Percent available one year policies end 1938
eightyeight point sixty return ninetyfour percent
end 1942 ninetysix point ten return ninetytwo end
March 1945 ninetythree point fortynine retuen ninety-
two confirming by letter.

MR. PARKER: Counsel have not had an opportunity to get together, and the suggestion is that we adjourn now, with the intention of having a meeting immediately after adjournment. When the hearing opens tomorrow morning we hope to be able to make a definite suggestion as to what is to be done.

THE CHAIRMAN: I should like to have an assurance

that we would conclude the insurance hearing tomorrow.

MR. PARKER: I do not think there is any question about that.

THE CHAIRMAN: This Commission has a great deal of administrative work to do, and as will have been observed, we have not had much time this week to do it. Perhaps we might begin somewhat earlier tomorrow morning, with a view to finishing this phase.

MR. MANN: I can assure the Commission that, so far as the stock companies are concerned, one hour is all that will be required at the outside. I do not intend to read a brief, and shall discuss only some general principles which, I should think, would require only about ten minutes. Then I intend to examine Mr. Ham on a few points which have not already been covered. There will be no repetition. Then, there will be one more witness on the question of the application of tax rates, and the question of relief, and that is all. The rest depends upon my learned friends, in whose hands, of course, I am. I can guarantee that, for my part, an hour will be sufficient.

MR. McKENZIE: On behalf of the Canadian Board of Marine Underwriters may I say that I have filed the statement of submissions of our organization. It is a very short statement and does not require any further argument on my part. I believe what I have set out in that brief is sufficient to make my point clear.

MR. MASON: There was some discussion earlier about argument at the conclusion of the hearing.

THE CHAIRMAN: I understand that matter is now going to be discussed with Mr. Parker, and that an announcement will be made tomorrow morning.

MR. MASON: Our difficulty at the present time is that, up to now, we have not heard from the joint stock companies. We shall hear tomorrow, I understand. Until we know what they are going to adduce before the commission, I do not think we can make up our minds as to whether we require argument and to what extent it may be required.

THE CHAIRMAN: I think you must know on what grounds they place their argument. Their briefs have been on the table for some days.

MR. MASON: I understand we are going to hear from two very intelligent and expert men, and we might learn something else after we have heard them. The point is that the matter is of considerable importance and, while I am not so much concerned perhaps as some of my colleagues who have somewhat the same interest -- because very little attack has been made upon me -- I do feel there may be matters of very considerable importance which my associates might wish to argue before the Commission.

THE CHAIRMAN: What I am hoping, Mr. Mason, is that there will not be oral argument. I am hoping that you will either agree that your briefs cover the situation, or that you will put in written factums.

MR. MASON: As an experienced judge you will know that a written argument is very unsatisfactory, because one does not know what is in the minds of the Commissioners.

THE CHAIRMAN: Even on the bench we realize that there must be a time limit. On Monday we are to discuss another subject entirely. Then, the Commissioners must have Saturday free for their administrative work. I am sure you would not want us to desecrate the Sabbath.

MR. MASON: I would not even suggest that you desecrate Saturday, sir. However, I raise this point on behalf of my colleagues and myself, because it had been understood earlier, after a conference with counsel, that there would be an argument, at which time we would have an opportunity to reply to the allegations made by the joint stock companies. All I can say is that if we have to close tomorrow such a procedure would be impossible.

THE CHAIRMAN: If you do not finish tomorrow, you cannot finish Monday; that is obvious.

MR. MASON: The Commission will understand our difficulty in making up our minds without first having heard from the joint stock companies.

MR. MANN: Do I understand that what is in Mr. Mason's mind is the form any subsequent argument may take?

THE CHAIRMAN: Whether oral or written.

MR. PARKER: And the form, and when.

THE CHAIRMAN: Whether there should be any argument at all, or whether it should be oral or written.

MR. HAYDEN: And if oral, when it should be heard.

THE CHAIRMAN: We cannot give you Monday, that is obvious.

MR. HAYDEN: If it is to be oral it will have to be at a later date.

THE CHAIRMAN: That is so. However, perhaps if you will get together and see what could be done by way of meeting everyone's convenience, it could be worked out satisfactorily. Then, it is suggested that we meet tomorrow morning at 9.30.

MR. PARKER: I am in the habit of meeting at nine, so that will be all right so far as I am concerned.

The Commission thereupon adjourned to meet
Friday at 9.30 a.m.

Canada Co-operative, Ry. Com. & Co.

ROYAL COMMISSION
ON
CO-OPERATIVES

1945

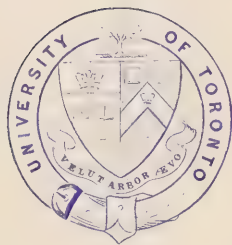
PROCEEDINGS
(OFFICIAL REPORT)



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ROYAL COMMISSION ON CO-OPERATIVES

Ottawa, Friday, April 20, 1945

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ROYAL COMMISSION ON CO-OPERATIVES

The Commission appointed to inquire into the present position of Co-operatives in the matter of income and excess profits tax, organization and business methods and operations, and the comparative position of persons engaged in business directly competitive therewith, met in Ottawa, on Friday, April 20, 1945.

PRESENT:

The Hon. Mr. Justice ERROL M. McDOUGALL, Chairman

B. N. ARNASON)	
G. A. ELLIOTT	(
J. M. NADEAU	)	Commissioners
J. J. VAUGHAN	(

Eugene T. Parker, K.C.	)	Associate
Roger Brossard, K.C.	)	Counsel

Major H. D. Woods	)	Associate
J. A. Chapdelaine	)	Registrars

Colonel G. W. Ross	)	Executive
	)	Secretary

APPEARANCES:

W. B. Francis	Group of Co-operative Associations
W. H. Howard, K.C.	Private Grain Interests
W. P. Fillmore, K.C.	Private Grain Interests
R. H. Milliken, K.C.	Saskatchewan Co-operatives
G. W. Mason, K.C.	American Reciprocal Association
V. Evan Gray, K.C.	Factory Mutual Fire Insurance Companies
Hon. S. A. Hayden, K.C.	American Mutual Alliance
N. S. Robertson	Ontario Cash Mutuals
Russell McKenzie, K.C.	Canadian Board of Marine Underwriters
J. A. Mann, K.C.	Joint Stock Companies
Aime Geoffrion, K.C.	
A. Leslie Ham	

Ottawa,
Friday,
April 20, 1945

The Commission met at 9.30 a.m. Mr. Justice McDougall presiding.

THE CHAIRMAN: Well, Mr. Parker, have you any report on the matter we were discussing at adjournment yesterday?

MR. PARKER: Yes, Mr. Chairman. I may say I discussed it primarily with counsel engaged in the insurance end of the commission work, and later with one or two of the others. There does not seem to be any unanimity of opinion or view as to just what would be the best way to dispose of it. The suggestion I make to the commission and to all concerned is this: that inasmuch as the grain hearings, judging from the appearance of the briefs, will likely take some time, and as certain work which the commission has in mind will occupy their attention after the grain hearings, I think the proper thing to do would be to have a considerable adjournment after the grain hearings are over and then set a date at some future time when everybody interested -- grain, insurance, and so forth -- might appear before the commission and submit such argument by way of summing up as they may see fit. If any counsel would prefer to submit written brief rather than attend and make oral argument, I do not see any reason why they should not have that election. In all deference to the commission I think it would be better if just before they are about to sit down and read all this mass of evidence that has been placed before them they have a summing up and argument of counsel so that it will be more or less fresh in their minds. I think that would be of great assistance to the commissioners at any rate, and I am sure that is what counsel have in mind in submitting

arguments -- no other reason than that of assisting the commission; and I believe they could render greater assistance at that time than at any other.

Now, I realize in saying that that it may be a matter of some inconvenience and some expense to counsel to have to return here again if it is their wish to dispose of the whole matter here. I am afraid there will have to be some inconvenience because the matter covers a very wide scope and it is almost impossible to meet everybody's convenience. I am sure, however, that the commission will endeavour to meet their wishes as far as possible. There is no desire to be arbitrary in the matter; certainly as counsel for the commission I have no intention of being arbitrary in the least degree. We have been cooperative up to date and hope to continue to the end on that basis. That is all I can say, Mr. Chairman.

THE CHAIRMAN: As I think most people know, this commission has made certain commitments which are coming along very shortly; and, speaking now of the insurance group, if it does not appear feasible to have any extended arguments to-day, we cannot finish to-day. Monday is to be devoted to the grain inquiry. I rather think that Mr. Parker's suggestion is very reasonable under the circumstances -- that is, that we conclude all the hearings, the grain trade next week, or whenever they finish, and then set a definite date when the commission will return to Ottawa for such arguments as may be found necessary -- if in writing, so much the better, but if not, oral. I would like an expression of opinion from counsel on that feature.

MR. MANN: I take it, Mr. Chairman, that if counsel optate to put in written argument instead of an oral argument in Ottawa, that would be a memorandum for the commission

and would not be subject to the rules of proceedings -- answer and reply, and so on, as it seems to have developed into at the moment.

THE CHAIRMAN: I take it that in that event it would be more in the nature of a factum than anything else.

MR. MANN: I quite agree with Mr. Parker's suggestion under the circumstances, so far as my companies are concerned.

MR. MASON: Mr. Chairman, we have thought it desirable to await the presentation by our friends this morning before determining whether we wish to present argument at all, or to leave it on the evidence as it is. I should like to mention the matter again after the presentation this morning is completed. If it seems desirable that argument should be made, then the question arises whether it should be oral or written. It is evident that the presentation of oral argument will be difficult both from the standpoint of the convenience of the commission and from the standpoint of the convenience of counsel. In that event it might be desirable to have written argument, on this hypothesis: that each counsel put in a memorandum once and for all, this memorandum to be filed at some time with the commission, and that there be no matter of reply. One further suggestion I would make would be that the commission might offer a bonus for concessions.

MR. GRAY: Mr. Chairman and gentlemen, what Mr. Mason has said expresses entirely my own view in regard to the suggestion that the commission has now under consideration. I rise simply to ask a question. In relation to the material that Mr. Glassco is to prepare from the factory mutuals material -- no doubt additional material will be provided for him -- will there be any opportunity to see his report and to make any comments either in argument or otherwise?

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THE CHAIRMAN: I would not think so, Mr. Gray. Mr. Glasco is one of the officers of the commission, and any information he gets for us is for the commission.

MR. GRAY: Well, perhaps there might be this understanding, then, as between Mr. Glasco and ourselves --

THE CHAIRMAN: I understood you were to discuss the situation with Mr. Glasco.

MR. GRAY: Yes, that would be quite satisfactory, as long as it is well understood by the commission that we may discuss the material with him in connection with the report that he makes on it.

MR. ROBERTSON: Mr. Chairman, I have nothing further to add to what Mr. Mason has said. My position is that taken by Mr. Mason.

THE CHAIRMAN: Mr. Parker, has this been discussed with the grain trade?

MR. PARKER: Only tentatively.

THE CHAIRMAN: Do you know about it, Mr. Howard?

MR. HOWARD: No, Mr. Chairman; we knew this discussion was going to take place this morning, and that is why we are here, to listen to it. Speaking for Mr. Fillmore and myself I would say that your suggestion is entirely satisfactory; that is exactly what we would prefer, and our idea would be to confine ourselves to further written submission rather than oral argument.

THE CHAIRMAN: That is, a factum?

MR. HOWARD: Yes, a factum.

THE CHAIRMAN: How about Mr. Milliken and Mr. Francis?

MR. PARKER: I had an opportunity to speak to Mr. Francis and Mr. Milliken last night. I outlined this view, which I told them I thought was the proper procedure to follow, and they said they would be quite agreeable to anything to

that the commission might suggest. I think up to that time they had had it in mind that the argument would go on immediately after the grain trade, but I would not want to commit them to that without giving them an opportunity to say so themselves.

Mr. FAYDEN: I am in agreement, Mr. Chairman, with what Mr. Mason has said.

MR. McKENZIE: I have no preference one way or the other.

THE CHAIRMAN: As I understand it, then, written briefs will be submitted, or there may also be oral argument?

MR. PARKER: If all counsel wish to submit written argument rather than oral, that is the end of it, and we do not need to worry about any date, except to fix a date before which they must have them in. If anybody wishes to make oral argument --

THE CHAIRMAN: Mr. Mason may be able to cover this point when the brief we are about to deal with has been heard.

MR. PARKER: Some counsel have expressed themselves definitely as wishing to have oral argument. They feel that written argument will not fill the bill.

THE CHAIRMAN: Well, we will deal with that later, then. Will you proceed with your brief, Mr. Mann?

Joint Stock Companies

MR. MANN: Mr. Chairman and gentlemen, I appear for 227 stock companies, all members of the All Canada Insurance Federation, 167 of whom are members of the Canadian Underwriters Association, all joint stock companies carrying on in Canada the business of fire, automobile and casualty insurance.

It has been observed by the companies and by myself that unfortunately we appear to have been put into a sort of quasi

position of prosecutors or persecutors with a view to the elimination of the competition of the Mutual Insurance Companies. I think it fair to assure the companies and the commission that these companies are a very large and influential body of the heart and nerve and commercial sinew of the dominion, and there is no desire whatsoever to operate in such manner or act in such manner that competition should be eliminated. They believe that competition is the life of trade, not the death of trade. There have been a lot of statements made in briefs which we pass over without any comment, with regard to the behaviour of these companies. I think we can leave it to the commission to decide as to the actual effect of it, or what it really means, or how much there is to it.

We have had considerable argument, both written in the briefs and verbal, in connection with the presentations of the cases -- Mr. Mason, Mr. Robertson, Mr. Hayden, Mr. Gray's Elegy, which no doubt will be continued in our next. They have been very instructive but they seem to be all encompassed by the feeling that the stock companies stand out as a great octopus of insurance operations within the dominion, with an attempt to put all the other fellows out of business, as it were. In that regard may I make this statement at the outset. As regards the farm mutuals, local, parish, who act as closely and operate as closely, and whose declaration of non-profit-making faith is borne out by their actions -- as to them we have no objection; we think they should remain free from contribution to the cost of government. I am excluding, of course, the local cost of government; I am now referring, so far as the cost of government is concerned, to income tax and war profits tax. There is always a line to be drawn when a mutual, so-called, ceases in fact to be a

mutual, ceases in fact to operate as a mutual. What we feel is, adopting the language of our friends the mutuals, that the public interest can only be served by the burden of government and the cost of government being carried fairly and squarely by all those operating as business enterprises, as profit-earning enterprises, in competition with each other. It is unfair that one body, by virtue of a declaration of faith, I repeat -- a declaration of non-profit-making faith which is entirely denied by the results -- should escape the cost of the services of the state from which they benefit, and that those services of the state should be paid for by others because they happen not to have made a declaration of such faith and because they are constructed in a little bit different form.

Now, that is begging the question as to what is profit-making, what are earnings, what are savings, what are surpluses. As to the distinction among them, I do not propose to burden you in the slightest degree with that; you have had weeks and months of it, and I am perfectly satisfied to leave it to the commission to determine whether there is profit-making, whether there are savings, whether savings are profits; when there are surpluses, if surpluses result from profits; that is something I can leave with the greatest confidence with the commission. But the attack or the criticism of Mr. Gray I do qualify by saying that if there is equal benefit from the state there must be equal burden.

I will take a few minutes, Mr. Chairman, to indicate to you what I believe to be the inequality, and, to put it colloquially, the unfairness of the incidence of the tax in respect of the actual operations of the mutual companies as compared with the joint stock companies. Perhaps the commission would not mind referring to schedule "C", for

example, in our first brief -- it is not paged, but it is fourth or fifth to the last schedule. It is not necessary to read it; I merely want to refer to certain figures for 1942 --

MR. PARKER: Which page?

MR. MANN: There is no page; it is schedule "C", the first brief. If you will look at the extract from the official blue books as to the year ended 31st December, 1942, you will see a compilation there of the reciprocals, the deposit-premium mutuals, other mutuals, stock mutuals, and joint stock companies. You will observe in the first column a premium income of the deposit-premium mutuals of \$1,275,072, with an underwriting profit of \$633,232; other mutuals, \$10,662,742, with an underwriting profit of \$1,336,245, and no excess profits or income tax paid -- none whatever. The stock mutuals, which are mutual companies -- using the word "mutual" -- or are organized under the joint stock principle and could by no stretch of the imagination claim exemption under the law as it is, are now taxed. You will observe a premium income of \$1,813,614 and an underwriting profit of \$56,516; excess profits tax, \$22,749, and total tax, \$49,461. But let me bring you to the next line: joint stock companies, premium income, \$82,919,000; underwriting profit, \$5,907,143. Then in the next column, excess profits tax, you will see the figure of \$2,710,706, and a total tax of \$4,303,452. There you have a tax of \$4,303,452 as against an underwriting profit of \$5,907,143, and you have the mutuals with \$12,000,000 and no tax.

The next one following down the page is the 1943 period. It is just as eloquent; the details are there and you can see them for yourselves. These are inequalities to which I am drawing the attention of this commission.

Let me refer now to schedule "G", three schedules further over -- and I may say to the commission that these inequalities are all I will burden you with this morning. You may see others; you may appreciate others or you may not; you may appreciate or you may not appreciate, but these are inequalities. Look at Schedule "G". For four years, 1940 to 1943 inclusive, you find that the premiums of the reciprocals were \$2,507,278, with an underwriting profit of \$726,510. Deposit-premium mutuals, \$4,028,594, with underwriting profit of \$1,841,641; other mutuals, premiums, \$40,698,630, with underwriting profit of \$4,959,348. The joint stock companies follow with very much larger premiums, it is true, but with a smaller underwriting profit-- premiums, \$326,493,837; underwriting profit \$20,185,502. Then if you look at the column headed "Taxes, including taxes on profits", you will see the figures; I do not need to read them to you -- they speak more eloquently than anything I can say. But if you look at columns 5, 6 and 7 you will see that they are totally blank with the exception of a minor matter of minus 52 cents -- I am not going to deal with that; and if you follow down to the joint stock companies you will find the staggering figure of taxes on profits of \$13,564,710.

These figures, Mr. Chairman, are from official records, and they are not competent to be contradicted, unless your commission feel it is worth while to have Mr. Finlayson brought here, or any of the other gentlemen here present think that he should be brought here to support or to deny these figures. I do feel, however, with the greatest confidence that these figures as they are now before you can be taken as they stand.

I omitted to say at the beginning that there are two mistakes which I should like to correct, in that certain paragraphs are to be deleted from the supplementary brief of the joint stock companies. I should have said this at the beginning; I am sorry. I refer first to paragraph (h) on page 26. I would ask you, Mr. Chairman, if you will completely delete this paragraph. It was prepared, and there were some errors in the figures; wrong figures were used, so I would ask you to ignore it completely. It may be necessary to reconstruct it, which we will do if we put in a written memorandum, or rather I think I should say when we put in a written memorandum. That takes us to Exhibit "H" at page 52 of the supplementary brief, which should be eliminated also. Those fit together, and they should be taken right out, and not read.

The All-Canada Insurance Federation is a body which is, in its essentials, legislative. The Canadian Underwriters Association is a corporate body which embraces, as I have said, 167 of these companies. It is essentially a plan-making and rate-making body. It might be well for the Commission to have that in mind; that the Canadian Underwriters Association, as a rate-making body, has been under investigation a good many times. It has its affiliations in other rate-making bodies in the states of the union, and operates on similar lines. It has its connection with the National Laboratories of Chicago; it also has its own laboratories. It has a very vast rate-making enterprise for the prevention of fire waste, the reduction of fire hazard and so on. Up to 1940 their plan-making organization -- these are figures I am stating from memory, but I do not think they are very far wrong, as appeared in certain litigation in 1940 -- their

plan-making organization had represented a cost of approximately \$14,000,000, altogether apart from additional costs, relative costs in connection with their rate-making, fire hazard reduction, education and other matters relative to the public interest in relation to fire hazard and fire risk.

In addition it has been frequently stated, and this is an impression that has gone abroad quite widely, that the Underwriters are a combination. They are; but, as the Chairman well knows, combinations have been stated many times, in the Supreme Court and particularly in the case which I referred to in which they were interested, as being useful. I believe in that case it was said that there may be a combination which is quite a useful and lawful combination.

THE CHAIRMAN: Beneficent is the word, is it?

MR. MANN: I say without the slightest evidence of doubt that this is the word, and I say that without any secret reservations.

There is just as much competition among the members of the Canadian Fire Underwriters Association and the Canadian Underwriters Association, which comprises fire, automobiles and casualty, as there is in any branch of insurance operations. The reason for that is perfectly plain. A schedule-rating system has been adopted by a large proportion of the states of the American union, because it puts the companies, in respect of themselves, as competitors, because of the very schedule-rating which they have introduced and upon which they operate, the general principle of which is this. A basic rate is fixed for a district as a minimum rate, which is the minimum only when the operations of the schedule do not come into play. But an astute agent who wants to get a risk knows his schedules. He knows that in the city of Toronto in 1923 -- I cannot give

the figures to-day -- there were 215,000 schedule-ratings. He knows that in Montreal in 1923 -- I cannot give you the figures to-day, -- there were something in the vicinity of 95,000 schedule-ratings. He knows that if he can go to the prospective insurer and tell him that if he puts an asbestos pipe around his furnace, or if he moves a bucket out into the yard, or if he cleans up a fence, or puts a door in a certain place, or takes down a wall, or puts something else in its place; or if he does something in respect of the furnace flue or stove flue, he will bring down the rate from 50 cents; two cents for one thing, one cent for another thing, three cents for something else, and five cents for something else, and by astute education of the assured he can get that rate down, for the purpose of avoiding fire waste, to perhaps 40 cents.

I ask this Commission: is he a public benefactor or is he not; and is that not beneficent? I put that to this Commission; and that need not be explained at the moment. It is a fact, and if my learned friends want to question Mr. Hurry when I come to examine him, he will be able to elucidate that very much better than I can.

This matter was taken into consideration in 1916 to 1918, and I do not think it would be unfair if I just read to you from the report of the Masten commission in 1916-1918, which was reported in 1919. I gave you my word I would not exceed an hour, and I will not do so. I believe I heard you, Mr. Chairman, ask for this report yesterday.

THE CHAIRMAN: Mr. Robertson filed a copy.

MR. MANN: I am not going to take time to read long extracts from it, but I want this evidence which will come in from these companies to go into five minds that are at

least impressed with what for two and a half years was the considered opinion of the late Mr. Justice Masten of Ontario, after a very full and long inquiry. I refer to page 10 of the report:

"I find that the idea is prevalent with many insurers of the province that the actions of the Canadian Fire Underwriters Association are arbitrary and autocratic, but my view is that the character of the work necessitates definite and precise rulings, and that these rulings not unnaturally appear to those seeking insurance arbitrary and autocratic."

I think perhaps that is the view of some of my friends in the room at the moment.

"My opinion is that if any complaint is warranted on this footing, it is that sufficient pains have not always been taken to make it evident to the insured that their representations have had full and fair consideration. I am of opinion, however, that the association is, at the present time, realizing more fully its position as being, to a large extent, that of a public service body, and is more fully appreciating the desirability and necessity of justifying to the insuring public the rates which it prescribes."

Now if the Commission will bear with me I should like to read on page 11; I will not take very long:

"The question that next arises is whether a combination such as the Canadian Fire Underwriters' Association is inimical to the public interest, and if so, in what direction or directions. It should be pointed out that a combine of insurance interests differs from a combine of grocers or manufacturers in certain important respects. In ordinary trade and commerce the selling price of all marketable commodities

is based upon known factors, viz., the cost of production, and the cost of distribution. The actual cost of insurance, on the contrary, cannot be determined until the lapse of the contract, and may be either a total gain or a total loss. Past experience affords the only guide as to what rates should be charged. The experience of one company or of many companies in a limited field, or over a short period of time, would obviously not give a sound basis on which to predicate rates. The only method by which there can be an even approximately equitable distribution of insurance cost is by combining the experience of many companies over a wide territory, and over a period of years.

"Again, it is obvious that the determination of proper rates would be valueless, unless steps could be taken to maintain them."

In 1922, in the courts of the province of Quebec, the finding of this commission in regard to the Canadian Underwriters Association was supported. The Exchequer Court and the Supreme Court of Canada supported those contentions which were raised all square in the Massey and Rennie cases, which were before the courts from 1937 until determined finally by the Supreme Court of Canada and the Judicial Committee of the Privy Council in 1941.

"It is a matter of experience that unrestricted competition between insurance companies has inevitably led to rate-cutting, and eventually to the failure or absorption of the weaker companies in the field. On the surface open competition may for a time appear to be in the public interest by reducing the insurance cost --"

I should like the Commission to note these words particularly.

"-- but even this is a doubtful benefit, owing to the discrimination in favour of large and influential insurers, which may, and undoubtedly does, prevail under such conditions. Under the system of schedule-rating where rates are properly maintained and enforced, discrimination cannot exist. The few instances brought to my attention during the course of this inquiry, were fully dealt with by the Canadian Fire Underwriters' Association, and appeared to me to be capable of reasonable explanation."

In case this Commission may be somewhat confused, I may say there were three associations prior to 1936: Canadian Fire Underwriters' Association, Canadian Casualty Underwriters' Association and Canadian Automobile Underwriters' Association, but those three were combined into one association, the Canadian Underwriters Association, by dominion charter in 1936, and the Canadian Underwriters Association operates as a corporation under Part II of the Companies Act, non-profit. It operates in three branches, automobile, casualty and fire. So the confusion between the Canadian Fire Underwriters' Association and the Canadian Underwriters Association is thereby cleared up.

"Whatever justification, however, there may be for a combination of insurance companies to maintain rates, there is undoubtedly the fullest justification for such a combination to limit the expenses of the business. There are obviously two ways of enlarging the turn-over of a company under competitive conditions -- one is to cut rates, and the other to increase commissions. From the standpoint of the insuring public, competition in respect to commissions is even more serious than competition in rates. In the event of rate reduction the public obtains at least a temporary benefit, but

in the case of increased expenses the public is invariably the loser.

"One of the strongest points in favour of an insurance combination such as the Canadian Fire Underwriters' Association, is the fact that its method of conducting business is not only economical and efficient, but incidentally brings about an improvement of conditions that directly benefits the public. The inspection of properties and schedule-rating, by which defects are brought to the attention of property owners, tends, in the long run, to effect a considerable betterment of the physical conditions which are largely responsible for the extent of our losses by fire. No individual company could maintain a staff of experts competent to give this service, without tremendously increasing the cost of insurance to the public. It is equally plain that no single company would be in a position to bring about improvements that can be effected by many of the companies acting in cooperation one with another.

"On the grounds which I have here set forth, I am of the opinion that the operations of the Canadian Fire Underwriters' Association have been and are to the advantage and in the interests of the public, and that such a combination tends strongly to maintain the solvency of the companies, to stabilize rates, to eliminate discrimination, and assist in controlling the expenses of carrying on the business.

"This conclusion accords with findings of the strongest commissions in the United States that have considered this question."

I am obliged to you, Mr. Chairman, for listening to me for so long in these extracts, but I thought it was very important, as a complete answer at least in so far as one

commission was concerned to the indictments that have been levelled at the heads of these companies. Then I want to read some very short extracts from pages 15 and 16:

"On the basis of the whole business transacted by all companies, out of every \$100 received, \$60.30 has been paid for losses, \$33.00 for expenses, and \$3.75 has been carried to conflagration and unearned premium reserve funds, leaving \$2.95 as the residue of premium income available for distribution by way of dividends upon capital stock."

Of course I have to be fair and say that was up to 1920. I think the aim of the companies to-day is to get approximately $2\frac{1}{2}$ per cent underwriting profit, and it will be explained to this Commission later on that if they get $2\frac{1}{2}$ per cent underwriting profit and pay 40 per cent income tax, they are paying an additional 1 per cent, which makes the difference between 2 per cent and 3 per cent so bitterly complained of by the mutual companies. That will be explained to the Commission in a few minutes. It must be perfectly clear that 40 per cent of $2\frac{1}{2}$ is 1, so you have the 3 per cent right away.

"Whether this is too much or too little I am unable to satisfactorily determine, but my immediate purpose in analyzing the above figures is to make plain the fact that by far the greater portion of the premium income collected by the companies is distributed in payment of fire losses and in general expenses, and that a comparatively small proportion of the premium constitutes the net underwriting profit."

I pause there to say this. Any distribution of general expenses must necessarily indicate to this Commission that somebody else gets the money. It must also indicate that with a nation-wide income tax, somebody else pays income tax out of the money they get from the distribution of expenses

by the underwriting companies.

"Consequently the most available avenues along which to advance in reducing the cost of insurance in Ontario, is to reduce the fire loss, and the expenses of carrying on the business. If all the divisible underwriting profit were wiped out, it would probably amount to less than 3 per cent of the premiums, whereas, if the fire loss in Ontario could be reduced by one-third, it would eliminate one-third of the loss incurred by the companies, and reduce the cost of insurance by approximately 20 per cent. . . .

"If the underwriting profits in Ontario are larger than are warrantable, having regard to necessary expenses and to the provincial fire loss, the remedy, as matters now stand, rests in the competition afforded by the non-board companies, licensed and unlicensed, and on the temptation to other companies to enter a new and profitable field. Having regard to the world-wide nature of the fire insurance business, to the keenness of competition, and to the fact which I have ascertained that those who are most intimately associated with the business rarely invest their surplus capital to any great extent in the stock of fire insurance companies, I incline to think that the profits are not excessive."

You will note and appreciate, Mr. Commissioner, that I am giving you this merely as the expression of very considered and reasonable opinion which is usual, I think, in quoting authorities which do not bind the court to whom you are quoting them. Now I continue quoting from page 17, dealing with agents:

"There is no doubt of the value and importance of the agent to the fire insurance business, and taking all things into consideration the agency system appears at the present

time to be best suited to the needs of our people in Ontario."

Of course this was limited to Ontario, but the general principles of course can be applied to all other parts of Canada, subject to certain local conditions. Then I continue quoting on page 18:

"The nature of the work performed by agents engaged in fire insurance varies very greatly, ranging from that of the skilled broker who writes extensive risks and examines the property to be insured, makes recommendations as to how the rate can be lowered and the risk improved; and on the other hand, the agent who merely receives the application for insurance on a dwelling sent in to him by the owner, makes no examination, and passes it on to the company after extracting as his commission, 25 per cent of the premium received."

That is a comparison between a good agent and a bad agent. The good agent assists the insurer in reducing the hazard, in comparison with the ordinary, happy go lucky, everyday fellow who just insures your house, takes his commission and says goodbye. Then I quote from page 28:

"One suggestion is that the Canadian Fire Underwriters' Association should maintain a larger staff of inspectors to periodically and continuously inspect ordinary unsprinklered risks and notify the owners of dangerous conditions and of improvements that ought to be made, cancelling risks where necessary if the suggestions are not adopted, and lowering the rate where that is warranted by the improvement made. I think that this suggestion is worthy of consideration and that if necessary an increase in rates sufficient to meet the cost of this additional inspection would not be objectionable to the insuring public."

Inasmuch as Mr. Justice Masten in his report referred to

associations in the United States, I want to draw your attention to just one other matter, and beyond that I will not bother you. I refer to the Illinois Fire Insurance Commission investigation of 1911. That was followed in 1923, I think, by a Senate inquiry, but unfortunately I have not the Senate report with me. I will read from the Illinois report, which was dealt with by seven men chosen by the legislature of the state of Illinois. I refer to page 51:

"The recent and general economic awakening has served to reveal the fact that competition is not the life of trade, but more frequently the death of it. Discrimination has run riot in our civilization because we were all nursed in the belief that 'competition is the life of trade,' without suspecting that, like most things, competition is a mixture of both good and evil. The competition which comes from a spirit of emulation and the desire to render better and more efficient service is in all respects good, but the competition that causes cut-throat strife in the effort to down each other is vicious."

Then I go back to page 49:

"So far as the making and application of basis schedules is concerned we find little or nothing to criticise, for in every respect this work seems to be entitled to be grouped with the laboratories, fire patrols, salvage bureaus, national fire protection and statistical associations, etc., as a beneficent --"

Those are the words of Mr. Chairman, which I find used here.

-- as a beneficent manifestation of the business, for under the application of these schedules every man may be said to

make his own rate, and in every direction it is possible to find improvements of hazard produced by schedule-rating."

Now, Mr. Chairman, I do not intend to read any more from the brief, nor will I burden you further with quotations.

Throughout the brief you will find confirmation of the principles asserted by these commissions, principles which I assert before you now with respect to competition, with respect to the reduction of fire hazard, in schedule-rating, and the reduction in fire insurance risks. I will necessarily have to put Mr. Ham in the witness box to satisfy the Commission, and leave anything else that has to be done to my learned friend, who may want to examine him.

Brief on Behalf of:

Joint Stock Companies carrying on in Canada
the business of Fire, Automobile and Casualty
Insurance, on the cash plan exclusively.

This brief is presented under the authority of an order issued by the Commission published in the press in Montreal on the 21st day of December, 1944, and necessarily does not purport to deal with the evidence or documents filed with the Commission, except such as Counsel may have been able to examine prior to its preparation and filing.

The words "Mutual" or "Mutuals" will be used throughout except to the extent that the context extends the intent of expression.

We have dealt with principles, which we believe the Commission should apply in its recommendations to His Majesty's Government for Canada, in so far as these principles relate to insurance organizations (other than life) calling themselves "Mutual", "Reciprocal" or "Co-operative."

We have not explored the field of cooperative farm and industrial organizations, except in so far as the principles governing their operations relate or are similar to mutual and so-called mutual organizations.

We believe that to a material extent the terms "Co-operative", "Reciprocal" and "Mutual" are interchangeable in respect of merchandising operations but these words have been, and are being professionally used in the description of organizations which have no relationship in their operations to strict mutuality or co-operation.

Order-in-Council P. C. 8725

In the mandatory provisions of the order-in-council the word "Co-operatives" is used to describe "organizations organized and operated on a co-operative or mutual basis

and organizations claiming to be organized."

The order states that there is doubt as to the general principles intended to be applied and the effect of the Income War Tax Act and Excess Profits Tax Act, 1940, in relationship to such organizations and that this doubt has created serious problems in connection with the administration of the taxing statutes and a measure of uncertainty in the business operations of some of the co-operative organizations; and that a public inquiry should be had in respect of the comparative position in relation to taxation under such measures of persons engaged in business in direct competition with co-operatives.

The Commission is consequently directed to inquire into the matters set out in (a), (b) and (c) of the Order-in-Council and to report all facts which appear to it to be pertinent for determining what would in the public interest constitute a just, fair and equitable basis for the application of these taxing measures to co-operatives and persons other than co-operatives, in respect of methods of doing business analagous to co-operative methods, and to make recommendations for the amendment of existing laws as they may consider to be justified in the public interests.

Types of Mutual Insurers

A.- Mutuals operated in accordance with the principles of mutuality:

(1) A, B and C agree among themselves that all will insure each, and for expenses of operation and upon the happening of a loss, each will contribute upon assessment. In such case there is no taxable income.

(2) A, B and C may incorporate and the corporation may act as a medium to incur the necessary expenses for operation and to collect contributions from A, B and C to a

common fund. Under such circumstances the surplus of contributions over losses and expenses is not taxable income (see Jones vs. South-West Lancashire Coal Owners Association, Ltd. (1926-27) Tax Cas. p. 790.) The revenue from interest, dividends, rents and other sources, such as re-insurance premiums, etc., however is taxable income in the hands of the corporation, inuring "to the profit of" the members.

(3) A, B and C may, instead of incorporating, appoint an individual to act as attorney-in-fact. This type of organization as in (2) above, has income from interest, dividends, rents or other sources, such as re-insurance premiums, etc., which is taxable as income, although under administrative practice this income is not assessed.

B- So-called Mutuals with taxable income:

(1) Those organized under Provincial Insurance Acts, which require the subscription of capital to a minimum amount: viz: A, B and C subscribe the capital and when the required capital has been secured the company commences to carry on business as an insurer. The company, once qualified to operate, then deals with anyone who is prepared to take out a policy for cash or render himself liable to assessment. The underwriting profit and all other income of such company is taxable.

(2) Such companies so organized have extended their operations in such a manner that their members as a group, being the owners of the company, have the company issue "non-assessable" policies to the public generally.

Therefore, A, B and C through their corporation are engaged in a business venture in exactly the same way as the shareholders of a stock company, and the underwriting profit and other income of the corporation is taxable; some such companies have now no assessment members, their total

business being on the cash basis only.

(3) In the Province of Quebec there are several companies known as Stock Mutuals, which up to 1940 were not assessed to income tax, in spite of the wording of section 4 (g), which excludes from exemption "Corporations having capital represented by shares." We believe that these companies now are assessed on their total income, except with respect to underwriting profit on their so-called mutual business. The exemption however applies to corporations that qualify for exemption and not to the alleged nature of the business transacted.

(4) The Province of Saskatchewan has made provision under part XIA of its Act for the incorporation of "Co-operative Insurers". The main distinction between a company incorporated under that section and a company incorporated under part XI (Mutual Insurance), is that the company under part XIA may be organized on a joint stock basis, which excludes it from exemption under 4(g).

C - Foreign Mutuals:

Foreign Mutual insurers may operate on any of the bases mentioned above or variations of them.

We suggest it is possible that a Mutual Insurer having accumulated large assets and reserves might adopt an underwriting policy of curtailing its business so that eventually the board of directors alone would be the sole policyholders or members. Under the present practice of assessment:

- (a) The corporation would not be assessed for income tax;
- (b) The directors would receive insurance in perpetuity free of cost;
- (c) They could have returned to them an annual payment as dividends on their policies, their proportionate share of

the earnings on the investments of the company; and,

(d) Such payments being policy dividends would inure to the benefit of the directors free of income tax in their hands.

On the other hand, if they so wished, they could wind the company up and receive their proportionate share of the accumulated assets and reserves, free from income tax.

The Income War Tax Act -- The Excess Profits
Tax Act, 1940:

To a material extent, both measures in their taxing sections are sufficient to meet the intent of Parliament, namely, taxation of income and excess profits.

Income:

Income is defined in Section 3 of The Income War Tax Act as the "annual net profit or gain or gratuity", etc., from any source whatever; consequently, all income is taxable.

The Excess Profits Tax Act, 1940, (section 2 (f) defines profits in the case of a corporation, as being those determined under the provisions of The Income War Tax Act and (section 2 (g) defines income in the case of other taxpayers, similarly. The latter Act however is applicable only to persons "carrying on business in Canada."

Exemptions:

The exemptions by the use of the word "income" seem to establish that all persons enjoying annual net profits and gains, unless exempted, are assessable to tax thereon under The Income War Tax Act and that all persons resident in Canada, carrying on business therein, are subject to tax under both measures, and are the following:

Under Income War Tax Act:

Sec. 4(g). Mutual Corporations - The income of mutual corporations not having a capital represented by shares,

no part of the income of which inures to the profit of any member thereof, and of life insurance companies except such amount is credited to shareholders' account.

Sec. 4(i) Farmers' Associations - The income of such insurance, mortgage and loan associations operated entirely for the benefit of farmers as are approved by the Minister.

Under Excess Profits Tax Act, 1940:

Sec. 7(a). This section includes the exemptions 4 (g) and 4 (i) of The Income War Tax Act.

Sec. 7(c). The profits of taxpayers other than corporations if the profits in the taxation period do not exceed \$5,000.00 before payment to partners or proprietors of salary, interest or otherwise.

Sec. 7A. Similar provisions in respect of small corporation profits.

Administration of the Taxing Acts

It will be seen at a glance that the taxing laws as at present in force are sufficient, if diligently applied, to tax all incomes of all persons including Mutual Insurers, both in respect of income when persons are not "carrying on business" and in respect of income and excess profits when they are. The administration of the exemptions however in The Income War Tax Act, Sections 4(g) and 4(i) and in The Excess Profits Tax Act, 1940, Section 7(a), 7(c) and 7A seems to have lost sight of the fact that all Mutual and so-called Mutual Insurers operating in Canada can and do have taxable income and excess profits.

In administering the law however it is not realized that if any Mutual Insurer has income that that income must of necessity inure to the profit of its policyholders, or members whether distributed, put to their credit or into a reserve account.

These organizations are bound to realize income and they are in fact carrying on business -- consequently are taxable under both measures.

It should be noted that the term "carrying on business" as used in the Excess Profits Tax Act, 1940, has a very much broader meaning than the word "trading" commonly used in England. The latter implies dealing in merchandise while under our legislation the words "carrying on business" imply doing practically anything which results in profits or gain.

Mutual, co-operative or co-operative owned or controlled insurance corporations which enjoy income and are carrying on business in Canada have not been assessed to income tax and/or excess profits tax; as regards unincorporated insurers, neither they as bodies nor their component members have been assessed to tax on the annual net profits and gains either of the body or of the members individually.

Similarity Between Mutual and Stock Insurance Operations

In general:

A Mutual Company

before transacting any insurance must:

1. procure incorporation
2. have sufficient working capital by membership subscriptions to meet the deposits required by the respective acts; at this point no insurance is in effect.
3. Procure a licence from the Superintendent of Insurance to transact the business of insurance.

A Stock Company

before transacting any insurance must:

1. The same.
2. have sufficient paid in share capital to meet the deposits required by the respective acts.
The same.
3. The same.

- | | |
|--|--------------|
| 4. begin the insurance business. | 4. The same. |
| 5. procure additional capital to
be paid in or make sufficient
profit the first year to meet the
unearned premium reserve after the
first year's business. | 5. The same. |
| 6. maintain similarly the necessary
reserves thereafter. | 6. The same. |

Both classes of investors are then entitled to a fair return on their capital from the profits of the business capable of being undertaken only after the required capital to do business has been provided, but only after Income and Excess Profits Taxes have been paid on such profits. No distinction can be made between assessments on capital stock not fully paid up and assessments on mutual subscriptions not fully paid up; nor between a partly paid stock certificate and an assessable note or subscription.

Any part of a Mutual obligation may be allocated to capital reserve exactly the same as a Shareholder's obligation is allocated to capital and a Mutual member is entitled to a fair return on capital, not as a policyholder but as an investor, the same as is a shareholder, out of the net divisible profits of the Company and at the discretion of the directors in both cases.

As soon however as insurance underwriting begins, the insurer has started the business enterprise for the carrying on of which the capital has been procured and through which income and profits are to be realized.

As to the Use of the Term "Mutual" in Insurance

All insurance contracts are in essence and substance "mutual" in the wider sense of the term, since it is the premium

iums of the many that pay the losses of the few. It is only incidental that in the case of Joint Stock Companies the original capital is subscribed by "shareholders" while the original capital of Mutual insurers is subscribed by "members". Subsequent accretions to assets in both cases is the result of skill in management and inures to the benefit and profit of the suppliers of the capital as well as to the policyholders.

The capital and reserves of both types of companies are the property of the Corporation, in the assets of which in the one case, the individual shareholders of the moment, and, in the other case, the individual policyholders of the moment, have "a right in respect of but not a right to." The assets in both cases are liable for the debts of the corporation and are disposable in the discretion of the directors and not of any individual shareholder or policyholder.

What mutual interdependence is there among assureds having risks in the same or different classes of business located from one end of Canada to another, and even beyond the borders of Canada, few of whom are known to each other, few of whom attend an annual meeting of the corporation; all of whom are only interested in securing their insurance at what they consider reasonable cost to them?

What mutuality of interest can there be between insureds of a mutual corporation, one buying fire insurance on his plant in Nova Scotia, another buying automobile insurance on his automobile fleet located in Winnipeg, and another buying fidelity bond coverage on his employees domiciled in Vancouver?

What mutuality of interest can there be between a farmer insuring his farm house and outbuildings against destruction and the large corporate manufacturer insuring his plant and equipment valued at a hundred or more million, or the insured which is a crown corporation or a provincial government or a municipality?

The fact is that between the mutual insurer and joint stock insurer there is little or no difference in method of operation.

Income of Mutuals

A Mutual Insurer must have a surplus of receipts over expenditures each year, unless it has a deficit.

This surplus is income:

(a) Interest from investments of the reserve or surplus funds is income of the Corporation; (this is freely admitted under all systems of law and jurisprudence);

(b) The surplus of premiums and assessment receipts over losses and expenses is also income and is "annual profit or gain from any other source;"

(I.W.T. Act, sec. 5.).

This income is taxable:

(a) It is the absolute property of the Corporation: a legal entity entirely different from members or shareholders: (Salomon vs. Salomon 1897 A.V. p. 22):

(b) The disposition of the surplus or reserve in the discretion of the Board of Directors or other named administrative body.

(c) In a mutual organization, to maintain the right with respect to any distribution of income, an assured must be a policyholder or member at the time of distribution; the termination of a policy contract extinguishes all rights not only under the contract but with respect to the accumulated assets of the Corporation. The same maintains mutatis mutandis, in the case of a shareholder in a stock company;

(d) The assets are attachable by the creditors of the corporation but not by the creditors of the policyholder or shareholder.

Dividends to PolicyHolders Cannot be
Deductible as Expenses

In distributing operating surplus by way of dividends to members, it cannot be said that such dividends are deductible as expenses because the company calls itself "Mutual" any more than they could in the case of a stock company.

The term "cost" or "cost of insurance" in the case of any insurer can be ascertained only with respect to its total business over a fixed period of time; an Insurer can only arrive at such a conclusion by totalling the losses and expenses over a fixed period of time and calculating the net earned premium income for the period and setting the one against the other. If they are equal, then on the average the premiums were precisely estimated. It would be putting coincidence to too great a test to expect any degree of precision with respect to each . and every branch of the business written, i.e., Fire, Automobile and the several branches of casualty. To suggest that within each of the classes of risks/ⁱⁿfor example, Fire Insurance, that the premiums for farm, mercantile and manufacturing business written, had been likewise precisely and accurately estimated to meet the actual costs, is beyond the realm of possibility.

It is clear that for some risks more is paid than is necessary to carry the class as such, while for other risks less is paid. Thus the surplus paid by some insureds is offset by the deficiency of others; but in paying dividends either to policyholders or shareholders this is not considered. In mutuals some policyholders because of membership get the advantage not only of obtaining their insurance at a rate inadequate for the class, but of getting a dividend for so doing.

Consideration of the time element in insurance contracts likewise confirms the impossibility of ascertaining the cost of carrying indemnity. Policies are written every day in the year and losses occur every day. The insurer must use a fixed period in which to calculate the surplus, say from January 1st to December 31st. The losses that occur during that period but prior to a person becoming a member affect the return that he will receive; on the other hand, his premium will affect the return of those who were members anytime during the period.

Not only are policies written and expire any day of the year, but they are written for varying periods, usually from one to three years. Furthermore, they are cancelled during currency by either party and at different rates of return premium, depending upon whether the insurer or insured cancels. In the former case unearned premium is returnable on a pro rata basis while in the latter case, the insured pays a penalty for cancellation; this penalty inures to the profit of the members who remain.

It is therefore impossible to say that a dividend is a return of excess of estimated cost over actual cost. The actual cost being impossible to ascertain, it cannot be said that a dividend is a return of excess of estimated over unascertainable actual cost.

From investment earnings current policyholders derive a benefit. To the extent therefore, that such earnings are considered in calculating the profit and loss of a Mutual Insurer, they distort any effort, futile though it be, to establish the actual cost to the insurer of carrying a risk, otherwise the cost of carrying a risk with an investment fund of five million dollars would be considerably less than the cost of carrying such risk by an insurer with an investment fund of

five thousand dollars.

Many mutuals issue what is known as "non-assessable policies." Such policyholders are not members and have no liability beyond their premiums and no hope of future dividends as members,

On "non-assessable" business there may be a profit and if so it inures to the profit of policyholders who are members. The portion of the profit on non-assessable business paid to a member (the assessable policyholder), is indistinguishable from a dividend paid to a shareholder of a stock company. The assessable policy as a group, like shareholders as a group, are therefore engaged in a business venture that may or may not produce a profit.

It is common practice for Mutuals to cede and accept reinsurances to and from other insurers. These are commercial transactions with non-members the same as if carried out by a Joint Stock Insurer. From such transactions, the Mutual insurer may make a gain or a loss. The gain, if any, will appear in its surplus, part of which may be distributed to members, or form part of the reserve held for their benefit or profit.

Therefore, the dividend paid by a Mutual Insurer to a member is not a discount -- a repayment of excess of estimate over actual cost of carrying the indemnity of such member -- but it is an arbitrary allotment of profit from a business venture.

Exemptions Amount to a Government Subsidy

Mutuals being free from taxation on their surpluses and investments can afford to allocate ^{to} the members and other assureds the amount of which the state has been deprived by reason of the exemptions.

The effect is clearly a state subsidy in favour of Mutual Policyholders or members, and its class discrimination to the disadvantage of all other Canadian taxpayers.

Here it may be well to indicate that it is only within the past twenty-five years that Mutual and so-called Mutual Insurance organizations have developed to the stage of vast commercial enterprise; this situation has come about progressively because of:

- (a) Gradual and unobserved departure from the field of true mutuality;
- (b) Failure on the part of administrative authority to appreciate the progression into the field of commerciality;
- (c) Political consideration involving the favouring of a vast body of individuals;
- (d) Failure by the legislature to examine the subject with a view to equalizing the tax burden on all taxpayers in the same or similar categories of business.
- (e) Insufficiency of localized tax inspection and determination.

Method of Procuring Capital for "Mutual" Operations

Mutuals operating in Canada like any joint stock company do and must have capital before they commence to "carry on business."

In all the provinces mutual insurers carry on business similarly to joint stock companies. The respective Provincial Acts invariably use the terms "carry on business", "income", "earnings," "profits", "surplus", "reserve", "assets", etc.

The effect of all the legislation with minor exceptions, is to require mutuals to have capital in some form before being issued a "licence to carry on business."

Mutuals as conditions preceding to operating must:

(1) Have in hand a given value in assets in the form of:

(a) cash and securities and)or;

(b) contracts by members to pay, called "premium notes."

(2) Make a deposit with the province (unless Federally licensed when the deposit is made with the Dominion Superintendent.

(3) Procure a licence to "carry on business."

(4) Set up a capital reserve or guaranteed fund (in which no member ever has an interest except upon liquidation), composed of:

(a) assessments of a percentage of members' notes;

(b) subscriptions to guaranteed stock.

Mutuals must thereafter:

(5) Maintain their unearned premium reserve fund according to the amount of insurance written and from time to time supplement their deposits (2)

(6) Maintain their capital (4) reserve by assessments from time to time.

(7) Maintain their general capital assets as required by the Superintendent.

None of the above has any relationship to the undertaking of insuring obligations, it covers merely the foundation or material upon which the structure of an insurance enterprise is to be built.

It matters not that a potential insurer in a mutual company gives a note for an amount admittedly many times greater than the premium, with the understanding that part of the proceeds is to be applied to capital reserve and part on account of the premium on the risk any more than if the same person gave a note to a Joint Stock Insurer with the understanding that part of the proceeds could be applied to his

stock subscription and part to his premium. In other words, what an assured of a Mutual pays in cash or as an assessment on a note as the consideration for the policy, is something distinct and different from his subscription to the capital of the Mutual, which latter subscription is in fact an asset of the corporation and the insured's investment in a business enterprise.

Mutual Organizations are Separate Legal Entities

A mutual corporation or association is an entity distinct from its members. (Salomon v, Salomon (H.L.) 97 A.C., p. 22)

They are independent organizations formed for the purpose of "carrying on business" for the purpose of gain.

(Arthur Average Assn. Ex parte Hargrove & Co.

10 Ch. App. 542 (1874-75)

(Padstow Total Loss, etc., 20 Ch. D.W. (1881-82) p.121.

(Cornish Mutual Assn. Co. vs. In. Rev. (1926) A.C.p.281)

(Municipal Mutual Ins. Ltd. vs. Hills (1932) 16 Tax Cas. 430)

As an entity distinct from its members, it of itself is subject to tax.

(Cornish Mutual Assn. Co. Ltd. vs. In.Rev.(Supra)

With respect to transactions with non-members, viz., returns from investments, re-insurance contracts with other insurers, and the issuance of policies to non-members there has never been any doubt in England as to a Mutual's liability for tax since such liability has been either conceded by the taxpayer or imposed by the Courts.

(N.Y. Life Co. vs. Styles (1899) 14 A.C., 381)

(Municipal Mutual Ins. Ltd. vs. Hills (Supra).

If income is earned, and Mutual Insurers in Canada do earn income both with respect to transactions with members and with

non-members, it matters not whether the income is disposed of to members as policy dividends or otherwise; it is subject to tax. The destination of the income earned is immaterial.

(Mersey Docks and Harbor Board vs. Lucas (1883)

8 A.C., p. 891.)

With respect to transactions with members, some transactions may be exempted but only where the Corporation acts as an agent for its members.

Styles' case decided that in life insurance when there was an undertaking to repay contributions made by members if they proved to be greater than necessary, the surplus was not taxable income.

In considering this case the distinction between life insurance and other classes must be appreciated. Statistics and actuarial formula permit of a close estimate as to the cost of carrying a life insurance risk, since apart from neglect to pay premiums a life policy must always become a claim either for:

- (1) the cash surrender value;
- (ii) the value at the end of an agreed period;
- (iii) on death,

so that periodical calculations as to cost can be made with reasonable certainty. On the other hand, other classes of insurance deal only with probabilities, not certainties, and no such calculation can be made with accuracy.

In the other than life field it has been held that where the members contribute to a fund in the hands of the corporation and the fund by agreement belongs to the members in proportion to their respective contributions, the company is merely a depository of funds placed in its hands under certain conditions and are repayable upon certain terms.

. In the case hereunder referred to the company was merely

a corporate agency to administer an agreement made by certain coal mine operators with a common interest in protecting themselves from employers' liability claims:

(Jones vs. S.W. Lancashire Coal Owners Assn., Ltd. (1927)
A. C., 827)

The common test of mutuality that there must be "complete identity between contributors and paryicipators" (Hills' case Supra) is not met by any Mutual or Reciprocal insurer in Canada, and would only be met were A, B and C to agree among themselves that all will insure each, and for expense of operation and upon the happening of a loss each will contribute upon assessment.

Suggestions as to Administration

The Commission has before it the reports of the Ritchie Departmental Committee, 1905, the Royal Commission 1919-1920 and the Lord Chancellor's Committee 1932-33, so that we will not refer to these reports in detail.

Inasmuch however as Mutual and Reciprocal insurance cannot be completely governed by the rules applicable to merchandising co-operatives, we suggest the following modifications of the Income and Excess Profits taxing measures as regards Mutual and Reciprocal insurers:

- (a) that all exemptions from taxation with respect to insurers in the other than life field be eliminated;
(I.W.T. Act 4(g) and (i);
- (b) that the tax on income and profits in respect of unincorporated bodies such as Reciprocal Exchanges and Inter-insurers who act through an Attorney-in-fact, be assessed to income tax upon the respective members, and that the Attorney-in-fact be assessed to income tax and excess profits tax in respect of the income and business profits of such organization remaining in his hands;

(c) that the recognition by Parliament that reciprocals and mutuals enjoy an advantage over the stock companies appearing from the differentiations in the premium tax, enacted by Sections 14 (1), (2) and (3) of the Special War Revenue Act 6 and 7 Geo. VI, Ch. 32, Sec. 5, be eliminated as being in no wise an equalizing measure and consequently that such sections be repealed; and/or that all insurers be put on an equal tax footing;

(d) that the Commission recommend that the administration of these measures be brought in so far as possible, into harmony with the provisions of the administrative sections of the Income Tax and Corporation Profits Tax branches of the British legislation.

Reference to Appendices

Appended hereto are Schedules "A" to "G" showing the highly unfair competitive advantage Mutuals and Reciprocals enjoy over Stock Companies and the consequent loss to the National Revenue.

These figures are taken from the respective official blue books and we venture the suggestion that it would be of advantage to the Commission when it sits in Ottawa to hear Mr. George D. Finlayson, C.M.G., Dominion Superintendent of Insurance, in respect to these figures.

Schedule "H" is a graph, the notes on which fully explain its purpose.

The Commission has had the advantage of a very full brief filed by the Income Tax Payers' Association, so that it will not be necessary that we repeat the reasoning of that body, which we adopt as ours in so far as its reasoning relates to Mutual and Reciprocal organizations.

In conclusion we draw the Commission's attention to the fact that while this brief is filed on behalf of

Joint Stock Companies carrying on business on the cash plan only, there are necessarily to be excluded Joint Stock Companies carrying on business on the cash plan which allocate part of the profits to shareholders qua shareholders and part to policyholders qua policyholders, and claim exemption from taxation on their incomes and/or profits on the ground that they are Co-operatives or Mutuals.

Respectfully submitted

Montreal, 3rd February,
1945.

J. A. Mann, K.C.

A. Leslie Ham,

Aime Geoffrion, K.C.,
Counsel.

For the Joint Stock Companies.

Supplementary Submission

on behalf of

Joint Stock Companies carrying on in Canada
the business of Fire, Automobile and Casualty
Insurance, on the Cash Plan Exclusively,
(except those claiming exemption from taxation
on the ground that they are Mutuals or Co-operatives)

"Apart from the necessity of commenting on the sixteen grounds suggested as sound for differentiating in taxation between Joint Stock Companies and Mutual and Reciprocal insurers, this supplementary brief is made necessary because of the fact that the submissions filed on behalf of The Factory Mutual Fire Insurance Companies, The Ontario Cash Mutuals, the American Reciprocal Insurance Association and the American Mutual Alliance, each attack in one way or another the Joint Stock Companies carrying on business in Canada.

"Part I

With respect to Grounds alleged as a
Basis for Tax Discrimination.

"The following grounds are alleged in one or more of the submissions of the Mutuals and Reciprocals in support of the contention that Mutuals and Reciprocals should not be liable to tax under the War Income Tax Act or the Excess Profits Tax Act.

1. That the nature of the ownership of the Corporation is the Determining Factor as to whether a corporation is subject to tax:

(a) Factory Mutual brief, p. 4:

"being wholly owned and controlled by their insured members."

(b) Factory Mutual Supplementary Brief, p. 8:

"In taxation matters, it is quite as wrong to regard corporations as separate from their ownership and control as it is to assimilate corporations which have different social and economic purposes to serve."

(c) Ontario Cash Mutual Brief, p. 3:

"A mutual company is the creature of and is owned by its policyholders only."

(d) American Mutual Alliance Brief, p. 3:

"The members own the mutual company."

(e) La Societe Mutuelle Brief. p. 3.

"Those companies are constituted by persons who have united without any intention of gain, but with a view only to protection."

IT IS SUBMITTED:

(a) That the control of the corporation by the membership

is not in fact an actual control, in spite of the statement to the contrary contained on page 7, Factory Mutual Brief: "The number of policyholders is small enough to ensure that the responsibility of the management to the policyholders is real and effective."

(1) The large membership precludes the likelihood of well attended meetings - 837 risks in Canada alone. (Factory Mutual Brief p. 8.)

(ii) The use of proxies at meetings lessens the certainty of control by the membership. (See section 3 Act of Incorporation quoted p. 9, Factory Mutual Supplementary Brief.)

(iii) "Were it not for the number of subscribers involved ^{being} and their/widely scattered it would not be necessary for the subscriber to pay anything until the end of the year's experience." (Reciprocal brief, p.3.)

(b) That the same membership of a Mutual corporation might at the same time be the sole shareholders of a Joint Stock Insurance Company which insured only the shareholders; such a corporation would not be exempt from tax under either the I. W. T. Act or the Excess Profits Tax Act on any such ground and furthermore the shareholders, if within the tax brackets, would be liable personally to tax on share dividends declared by such corporation.

(c) That all systems of law recognize that a corporation is separate from its members.

Therefore, it cannot be said that the particular persons who own a corporation is in itself the test as to the liability of a corporation to tax. The only exemptions on the basis of ownership of a corporation recognized by the I. W. T. Act are:

Section 4(d) - Municipal undertakings;

Section 4(m) - Reciprocal shipping income tax exemption;
Section 4(n) - Dividends from wholly owned subsidiary
non-resident companies.

And the maxim "inclusio unius est exclusio alterius"
applies.

2. That a Mutual Insurer Deals Only with its own Members:

(a) Factory Mutual brief, p. 2:

"So far as the Factory Mutuals are concerned, these
insurers have no insurance obligations to any per-
sons other than their own members and do not collect
premiums from any persons except their own members."

(b) American Reciprocal Assn. brief, p. 2:

"Each subscriber gives a power of attorney to the
common attorney to transact the necessary business
on his behalf."

(c) Ontario Cash Mutual brief, p. 3:

"is owned by its policyholders only; it functions
to protect its policyholders against loss."

(d) American Mutual Alliance brief, p. 4:

"Every policyholder is a member of the corpora-
tion and no policies are issued to non-members."

(e) La Societe Mutuelle brief, p. 2:

"The associates are both insured and insurers.
They are called upon, as insurers, to indemnify
their associates in case of loss; as insured, they
are entitled to an indemnity from the association
if they become victims of a loss."

It Is Submitted:

(a) That if the charter of the corporation or the statute
under which the corporation is created states that all custom-
ers are members, how in the nature of things could it be
otherwise?

(b) That under such circumstances a proviso such as is found in section 4(p) I. W. T. Act limiting non members' business to 20 per cent would be meaningless.

(c) That in the end, the result is the same as that achieved by the Northern Alberta Dairy Pool Limited. (See reply of Mr. Stanley to Counsel, p. 934 and to the Chairman of the Commission, p. 936, vol. 3, Official Reports of the Proceedings of the Royal Commission on Co-operatives.

(d) That in a type of mutual insurer where all or part of the business is written on a "fixed cash premium" basis, policyholders on such basis are not in the proper sense members of the corporation, irrespective of whether the memorandum of association or charter declares them to be so, since there is no liability for the debts of the corporation although there may be a right to share in the profits or operating surplus at the discretion of the board of directors, i.e. the test of Lord Watson in the Styles case, 14 A.C., 381, is not fulfilled:

"Each and every holder of a participating policy becomes ipso facto a partner of the company with a voice in its administration and entitled to share in its assets and liable for all losses and expenses incurred by it."

(e) That in the case of all Mutuals and Reciprocal, the above test is not met since the liability of the policyholder for losses and expenses is limited either

(i) by being a policyholder on a "fixed cash premium" basis, e.g., Ontario Cash Mutuals, their brief pages 2 and 3, the American Mutual Alliance, their brief, page 4;

(ii) by a contractual limitation of liability in the policy itself, say five or ten times the amount of

the cash premium, e.g. The Factory Mutuals, their brief, p. 9, The Reciprocals, their brief, exhibit 1, par. 6;

(iii) by premium note of a policyholder for a sum certain being a percentage of the amount of risk, e.g., La Societe Mutuelle, their brief, p. 4. See also the examination of Mr. Barrett-Leonard, p. 387, vol. 1, Official Report of Proceedings of the Royal Commission on Co-operatives.

Therefore it cannot be said that those who are the customers or patrons of a corporation, is itself the test as to the liability of the corporation to tax. The exemptions on this basis are recognized by the Statute:

4(i) - Farmers Associations - must be operated entirely for the benefit of farmers and be approved by the Minister.

4(p) - Co-operative Companies and Associations - non membership patronage must not exceed 20 per cent in value.

4(q) - Banking Institutions - patrons must reside mainly within the province.

Again the maxim "inclusio unius est exclusio alterius" applies.

3. That the Policyholders of a Mutual Corporation are Self Insurers:

This contention is repeatedly made in the brief of the Factory Mutuals, pp. 1, 2, 4 and pp. 21 to 23.

(a) Factory Mutual Brief, p. 2;

"Mutuals and reciprocals are self insurers."

(b) Factory Mutual Brief, p. 21:

"The only difference between insurance provided by the Factory Mutual Companies and the owner of property who insures himself - that is, carries his own risks - is that

in the one case, the protection is provided in corporation form whereas in the other it is done individually. In both cases they are self-insurers."

(c) Factory Mutual Brief, p. 22:

"If it functions as a voluntary association without purpose of profit, all for the benefit and protection of its members, then there is no more reason why it should be included within the provisions of income tax laws than there is to tax an individual manufacturer who carries his own risks - insures himself - and creates reserves for that purpose."

(d) Factory Mutual Brief, p. 24:

"In such circumstances adequate contributions to reserves are as proper and necessary deductions from income as are actual losses paid."

It is Submitted:

(a) That neither the I. W.T. Act nor the Excess Profits Tax Act exempt funds of taxpayers appropriated by them for the purpose of self insurance. Such appropriations are not deductible as expenses nor are the earnings on such appropriations exempt from taxation.

(b) That "A" is a self insurer and places \$10,000 per annum in the insurance fund; in order to do so he must earn $\$10,000 \times \frac{100}{100 - \text{tax rate}}$. The larger the fund, the higher the earnings on it and therefore the higher the tax rate against "A's" whole surplus, and the more "A" will have to earn to produce \$10,000 net for the fund. "A's" tax bracket is higher by virtue of the earnings on the fund and will tend to increase with each \$10,000 deposit made into it.

(c) That "B" insures in a Mutual, pays a premium of \$10,000 and this is deductible by "B" as an expense.

Because the Mutual is tax exempt, the earnings on the investment of \$10,000 in the hands of the Mutual is free of taxation.

Expenses of the Mutual for management may be paid out of the investment earnings and the balance is returnable to "B" and by reducing the \$10,000 premium and expenses by the amount returned, "B" is subject to higher tax.

But "B"'s tax bracket was lowered by the payment of the \$10,000 in premium and is only raised by the amount that is returned to him.

I.E. the interpretation of a Mutual Insurance Corporation between the taxpayer and the exchequer achieves a saving for the taxpayer. On the other hand, the interjection of a corporation by "A" through the investment in stocks or bonds for deposit in the insurance fund adds the imposition of another tax.

Therefore it cannot be said that this is a ground for exemption even if the allegation itself were true that "the situation here is no different than is that of the individual who insures himself, establishes and maintains a fund for that purpose, and invests it and receives income from his investment." (Factory Mutual Brief, p. 23.)

4. That the Policyholders act in Two Capacities, That of Insurer and Insured:

(a) Factory Mutual Brief, p. 9:

"During the life of the policy, each deposit is charged each month with its pro rata share of the losses and expenses and contributions to reserves."

(b) Factory Mutual Supplementary Brief, p. 9:

"It has often been said in adjudicated cases that in

mutual insurance companies, policyholders are both insured and insurers. That is true in the final analysis in the case of the Factory Mutuals."

(c) American Reciprocal brief, p. 2:

"The attorney collects moneys from each subscriber which are placed to the credit of the subscriber and remain the property of the subscriber. The attorney deducts from this amount such sum as may be required to pay losses and expenses and provide necessary reserves and surplus."

(d) American Reciprocal Brief, p. 3:

"He makes a deposit out of which his proportionate share of losses and expenses is paid."

(e) American Reciprocal Brief, p. 8:

"The liability of subscribers is not joint but several. Each subscriber secures insurance in severalty from the other subscribers and is in turn liable in severalty to each subscriber."

(f) Ontario Cash Mutuals, p. 3

"The mutuals came into being from necessity as a banding together of property owners whereby fire losses suffered by the few would be borne by the many."

(g) La Societe Mutuelle Brief, page 2:

"The associates are both insured and insurers."

It Is Submitted:

(a) That this relationship does not exist in fact since the contract is made between each policyholder and the corporation and not each policyholder with the other, save with a possible exception in the case of Reciprocal.

(b) That on the other hand, if it could be said that a policyholder does act in the capacity of an insurer, then

he in that capacity engages in a business venture supplying capital for such venture (Joint Stock Brief, p. 5.)

(c) That the allegation referred to in section 3 above, that mutual policyholders are self insurers, is incompatible with the contention that such a policyholder is an insurer of his fellow members rather than of himself.

Therefore, if it is a fact that a policyholder or subscriber is an insurer, he is liable to tax on this activity under section 3 of the I. W. T. Act reading "income means the annual net profit or gain or gratuity" ... " as being profits from a trade or commercial or financial or other business."

5. On the alleged ground that agency relationship exists between the Policyholder and a Mutual Corporation:

(a) Factory Mutual Supplementary Brief, p. 23:

"The Factory Mutual Company is a corporate agency of the policyholder and indistinguishable from him and his interests."

(b) Factory Mutual Supplementary Brief, p. 7:

"Neither indeed have they any property or possessions to be taxed, except property and possessions belonging in truth to some natural persons whose legal instrument or agent is the corporation."

(c) La Societe Mutuelle Brief, p. 10:

"The society is consequently only the depositary, the fiduciary of the savings made on the insurance transactions."

It Is Submitted:

(a) That this contention is incompatible with that in section 3 above, i.e. that policyholders are self insurers since to create an agency relationship requires two parties, not one.

(b) That there is no ter, in the mutual insurance policy that creates the relationship of agency.

(c) That there is nothing in the conduct of the parties that creates such a relationship.

Therefore, it cannot be said that the said taxing statutes do not apply on this ground.

(6) On the Ground That the "Form of Organization" is the Determining Factor as to Whether a Corporation is Subject to Tax.

(a) Factory Mutual Brief, p. 7:

"The Companies have no capital stock and no shareholders."

(b) American Reciprocal Brief, page 2:

"There are no shareholders or third persons interested in deriving a profit from the operation of the exchanges."

(c) Ontario Cash Mutuals Brief, p. 3:

"A mutual company is the creature of and is owned by the policyholders only . . . A stock company on the other hand is the creature of and is owned by its stockholders."

(d) American Mutual Alliance Brief, p. 3:

"It has no share capital or shareholders."

"The members own the mutual company."

It is Submitted:

a) That under the statutes of the several provinces of Canada insurers may be organized:

(i) with share capital

(ii) without share capital (Mutual)

and some provinces permit the operations of individuals operating under a plan known as Lloyds;

(b) That in each case capital is a necessary condition precedent to the "carrying on of business". (See Joint Stock Company brief, p. 9.

(c) That section 4 (g) I.W.T. Act does not exempt:

- (i) Mutual companies "having capital represented by shares; or
- (ii) Mutual companies "the income of which inures to the profit of any member." (See admission, Factory Mutual Brief, p. 7):

"No portion of the earnings of these companies remaining after providing for operating costs and reserves can enure to the benefit of anyone other than the policyholders."

(d) That Mutual corporations do have income from:

- (i) investments; rents, interests and dividends;
- (ii) re-insurance contracts with other insurers;
- (iii) penalties exacted from policyholders for cancellation of policies prior to expiry.
- (iv) surplus of premiums collected over losses and expenses paid out.

(e) That all of such is income within section 3 of the I.W.T. Act.

(f) That said mutual insurers are either persons "residing or ordinarily residing in Canada", or are "carrying on business in Canada." (section 3, Excess Profits Tax Act)

(g) That the policyholders of the moment, i.e. the owners of the Mutual company at the moment are not identical with the policyholders who have contributed to the assets of the company over the years.

(h) That with respect to joint stock and mutual form of organization, capital is necessary. (See Joint Stock Companies brief, p. 9.)

(j) That in each case, capital either supplied by share subscription or earned reserves or both, is supplied by persons;

(j) That the difference in form of evidence of interest in the corporation, (i.e. a share certificate on the one hand and an insurance policy on the other) is not a sound ground for distinction in liability to tax.

Therefore it cannot be said that the "form of organization" is the determining factor. The real test as to liability of a mutual corporation to tax is not the "form of organization" but whether the organization is a resident of Canada or carrying on business in Canada and if so, whether it has income from any source and if it has income whether it "inures to the profit of any member" of such organization, unless otherwise specifically exempted by the statutes.

7. On the Ground that the "Purpose" of the Organization is the Determining Factor as to Whether a Corporation is Subject to Tax.

(a) Factory Mutual Supplementary Brief, p. 4.

"Talk about equality of taxation, in such a variety of form and purpose of business organization, is oversimplification ..."

(b) Factory Mutual Brief, p. 2:

"Mutuals and reciprocals are self-insurers, organized and conducted by policyholders for their own benefit.

(c) Reciprocals, brief, p. 2:

"Their purpose is to provide a high degree of security to the subscribers at the minimum of cost."

(d) Ontario Cash Mutuals, brief, p. 3:

"A mutual company seeks to give protection and reduced rates as nearly to cost as possible."

(e) American Mutual Alliance brief, p. 3:

"The mutual company member is interested, first in the insurance fund being sufficiently solvent to provide sound insurance protection and, secondly, in securing his insurance protection at the lowest cost"

(f) American Mutual Alliance supplementary brief, p. 3:

"The test, it is submitted, is and should be not what the company calls itself but rather what the intention was from the outset."

(g) La Societe Mutuelle, p. 3:

"It is not the aim of mutual insurance companies to make profits to be divided among the partners or to benefit the company itself."

It is Submitted:

(a) That the "purpose" of the organization should not generally be the test as to liability of the citizen to tax since:

- (i) the expressed or alleged purpose may never be achieved;
- (ii) if achieved in whole or in part, in the achievement of it other results may follow:
 - (1) Although one's purpose may not be to make a profit, a profit may be made;
 - (2) The professed object "to achieve a high degree of security at minimum cost", "to give protection at reduced rates" or "provide sound insurance . . . at lowest cost" may and likely does result in a profit.
- (iii) Most citizens would claim that they serve the community and fulfil a true social function, but such claim or fact does not of itself exempt such citizens from tax; the doctor,

the nurse, the judge, the legislator are not exempt on the ground that they serve a social function. The purpose served by individuals is acknowledged by the I. W. T. Act with respect to only:

section 4(t)
4(v) Service pay and allowances;

section 4(w) Merchant Marine;

section 4(x) R.A.F. Transport Command

Again the maxim "*inclusio unius est exclusio alterius*" applies.

(b) That the Parliament of Canada contemplated the creation of non profit corporations, i.e. corporations "for the purpose of carrying on in more than one province of Canada, without pecuniary gain to its members, objects of a national, patriotic, religious, philanthropic, charitable, scientific, artistic, social, professional or sporting character or the like." (See Part II, sec. 140, ss. 1, Act respecting Dominion Companies, 24-25 Geo. V, cap. 33.)

Sub-section 2, however, provides "nothing in this Part shall be constituted to authorize the corporation . . . to engage in the business of banking or insurance."

- (i) It is to be noted that in spite of the pleas contained in the several briefs with respect to the social value served by mutual insurers, that the Parliament of Canada specifically excluded the field of insurance from objects for which corporations might be created under Part II of the said Act.
- (ii) The mere fact that a corporation is incorporated under Part II would not per se prevent such corporation from making a profit; if it in fact made a profit it would be taxable.
- (iii) If it is to be noted that under section 4(g) of the I.W.T. Act, corporations organized under Part

II of the Act are not exempt on that ground.

Therefore as the I.W.T. Act does in specific instances acknowledge the "purpose" of an individual as set out above and of an organization or corporation as a ground for tax consideration as follows:

- 4(e) - Charitable institutions;
- 4(f) - Labour organizations;
- 4(h) - Clubs;
- 4(i) - Farmers Associations;
- 4(p) - Co-operative Companies and Associations;
- 4(y) - Limited Dividend Housing Corporations;

all of which are subject to qualifications as in those subsections set out, a general right of exemption on the ground of "purpose" cannot be sustained either for individuals or corporations, i.e. the maxim "inclusio unius est exclusio alterius" applies.

8. On the Ground that to tax Mutual Organizations would be Contrary to Public Policy or Public Interest:

(a) Factory Mutual Supplementary Brief, p. 4:

"The co-operative and the public authority may, on grounds of sound public policy, be exempt from taxation."

(b) Factory Mutual Supplementary Brief, p. 4:

"and this Commission is charged with the consideration of public interest as a basis of fiscal policy"

(c) Factory Mutual Supplementary Brief, p. 6:

"The briefs filed by our competitors ... seem to have ignored the economic, social and political considerations of public interest which any tax proposals must involve."

(d) Ontario Cash Mutuals Brief, p. 20:

"It is submitted that it is not in the public interest to impose taxes which can possibly have the result of preventing the development of mutual insurance.

(e) Ontario Cash Mutuals brief, p. 24:

"That it is not in the public interest to apply or attempt to apply the Income Tax and Excess Profits Tax Acts to Cash Mutual Companies."

It is Submitted:

(a) That the terms "public policy" or "public interest" have no precise meanings. The meanings of these terms vary with time and place and circumstances and have never been delineated with precision by any court or legislature in this country.

(b) That all the briefs filed with the Commission contain only statements as to what the authors of the briefs consider to be public policy or in the public interest.

(c) That there can be no argument against the proposition that "the Commission is charged with consideration of public interest as a basis of fiscal policy."

(d) That in the last analysis, the point to be determined is whether it is in the public interest:

(i) that other things being equal there should be a tax discrimination between competitors;

(ii) that a tax policy should be pursued which has a tendency, through discrimination between competitors, to eliminate taxpayers from business and commercial enterprise;

(iv) that a tax policy should be pursued that levies the cost of government (and at present the additional cost of the war fought for the

benefit of all) on the shoulders of some and as between competitors burdens one and subsidizes another.

Therefore it is begging the question to found an argument on the words "public policy" or "public interest" until it is ascertained just what is "public interest" or "public policy" in this particular case.

The Commission's special attention is directed to extracts from:

Report dated January 18, 1919, of the Ontario Insurance Commission, 1916-1918; and

Report dated January 4, 1911, of the Illinois Fire Insurance Commission to the Senate and

House of Representatives (Senate Joint Resolution 24.) which will be found in Exhibit "A" attached hereto.

9. On the Ground of while a Mutual Corporation is Admitted to be a legal entity, it is alleged it is not separate and distinct from its members:

(a) Factory Mutual Supplementary Brief, p. 8:

"There are times when the legal fiction, called a corporation, can be discussed as such, but when discussing taxation, it is quite wrong to speak of corporations as separate and distinct from the members thereof, since even a superficial inquiry soon discloses that every corporation is owned and controlled, directly or indirectly, by some natural person or persons who have a specific purpose to serve through its activities."

(b) Factory Mutual Supplementary Brief, p. 8:

"In taxation matters, it is quite as wrong to regard corporations as separate from their ownership and control as it is to assimilate corporations

which have different social and economic purposes to serve."

(c) Factory Mutual Supplementary Brief, p. 9

"While it is true that the Factory Mutual Companies are legal entities, it is not true that they are separate and distinct from their members."

It is Submitted:

(a) That any corporation is an entity distinct from its members; (Salomon vs. Salomon (H.L.) 97 Appeal Cases, p. 22.)

(b) That it is improper to say a thing is an entity for some purpose and not for others.

Therefore as the Income War Tax Act and Excess Profits Tax Act tax income irrespective of the nature of the person who earns it, i.e. "person includes any body corporate or politic and any association or other body", the test is, did such person:

(i) earn income?

(ii) if so, is it exempt by the terms of the statutes?

10. On the Ground That to tax a Mutual Corporation would be to Tax on the same income twice:

(a) Factory Mutual Brief, p. 7:

"As for the Factory Mutuals, if they returned to Canadian policyholders their savings in the cost of fire insurance, with the effect that these policyholders were able to reduce their expense and pay higher

income and excess profits taxes to the Dominion Treasury, whose was the greater contribution to Canada's economic stability and fiscal solvency . . ."

(b) Reciprocal Brief, p. 2:

"Nearly all of the subscribers are corporate bodies but in the case of all subscribers the moneys paid to them by the attorney each year are subject to income tax and excess profits tax so that a further imposition of such taxes on the moneys of the subscribers in the possession of the attorney would mean double taxation."

It is Submitted:

(a) That if a Mutual should have paid X dollars in taxes but in fact distributed this amount by way of dividends to policyholders, the exchequer will not receive X dollars in taxes from the policyholders, since:

(i) only policyholders "carrying on business" and thereby entitled to deduct premiums as expense would have their taxable income affected in favour of the Crown. Policyholders not "carrying on business"

receive the dividends free of income tax in their hands although a portion of it is made up of interest earnings on the reserves of the mutual corporation;

- (ii) those carrying on business who deduct insurance premiums as expense would only pay the tax percentage on the portion of X dollars that they receive;
 - (iii) it is conceivable that the Crown might get nothing because it might happen that no policyholder, whether 'carrying on business' or not, was in fact within a tax bracket.
 - (iv) with respect to those 'carrying on business', the reverse of the argument is true, i.e. that if the corporation were taxed as such, its dividends would be less, the return to the policyholder being smaller, the expense item would not be reduced as much and the tax would be less;
- (b) That with respect to the statement 'whose was the greater contribution to Canada's economic stability and fiscal solvency', the question is repeated because out of the premium dollar paid to a joint stock company
- (i) part is paid to Canadian agents who are Canadian taxpayers;
 - (ii) part is paid by the companies themselves as taxpayers;
 - (iii) joint stock companies maintain large staffs in Canadian offices and part is paid to Canadian staffs who are taxpayers maintaining large offices in Canada;
 - (iv) part is paid to Canadian landlords and suppliers of Canadian service, all of whom are Canadian taxpayers.

(See Exhibits 'B' and 'C' showing taxes (excluding Income and Excess Profits) and expenses (excluding losses and commission) paid in Canada by Factory Mutuals and British and Foreign Companies having a comparable premium income re 1938 Fire Business and 1943 Fire Business, being the last year before the war and last figures available.)

Therefore as at the moment Parliament has not deemed it inappropriate or improper to tax income first in the hands of a corporation and again in the hands of the owners of the corporation, the argument by one corporation that it is justifiable when applied to its corporate competitor but not when applied to itself, is at least open to the charge of inconsistency.

11. On the Ground that Factory Mutuals Offer 'Engineering Services' which tend to Curtail Fire Losses in the Interest of the Community.

(a) Factory Mutual brief, p.1:

'But some insurers do differ from others by adding to this fundamental service of collection and distribution of money, an active engineering service devoted to prevention of loss from certain insured perils such as fire and explosion.'

(b) Factory Mutual brief, p.7:

'The object is prevention of loss by fire, through continuous expert engineering service, and indemnity of members for loss by fire and allied risks.'

It Is Submitted:

(a) That while this is of value to the community, it is not a sound ground of tax exemption.

(b) That such service is largely, if not entirely in the case of the Factory Mutuals, limited to the policyholders of such companies.

(c) That Joint Stock Companies render a similar or superior service not only to policyholders but to the community as well by way of inspection of and grading of

(i) Municipal water supplies and waterworks;

(ii) Municipal fire and police establishments.

See reference to such reports by W.J. Scott, K.C.,

Fire Marshall, Province of Ontario, - Exhibit 'D'.

(d) That the value of such inspection by Joint Stock Insurance organizations may in part be estimated from the following:

(i) Ontario Insurance Commission, 1916-1918, See Exhibit 'A';

(ii) Illinois Fire Insurance Commission, 1911 - See Exhibit 'A';

(iii) Report Illinois Senate Committee, 1923, pp.4, 5, 9.

(iv) Exhibit 'E' showing:

The offer to the Dominion Government of the engineering facilities of the associations. Letter from A.H.S. Stead, Manager of the Dominion Board of Insurance Underwriters, to Dr. E.H. Coleman, Under-Secretary of State.

Pursuant to said offer, such associations have made 3968 inspections in the years 1941 to 1944, both inclusive, for the Department of Munitions

and Supply; acted as consultants and made inspections of harbour installation, camps and training centers and ordinance stores, on behalf of the Navy, Army and Airforce.

(v) Exhibit 'F':

An acknowledgment of the value of these services.

Letter from Hon. C.D. Howe, Minister of Munitions and Supply, to Hon. J.L. Ilesley, Minister of Finance.

(e) That Joint Stock Companies themselves would hesitate to urge that the rendering of such services is a reason for tax exemption appreciating that most citizens in pursuit of their avocation render comparable services to the community either as an end in itself or as a matter of public relations.

"Therefore and in view of the fact that section 4, I.W.T. Act takes cognizance of certain types of community service as a ground of exemption but does not exempt such services as referred to above, this cannot be said to be a sound ground upon which to appeal for exemption.

See section 4(e) - Charitable institutions;

" 4(f) - Labour organizations, in part;

" 4(h) - Clubs, in part;

" 4(t)
)- Service Pay and Allowances;
4(v)

" 4(w) - Merchant Marine;

" 4(x) - R.A.F. Transport Command;

" 4(y) - Limited Dividend Housing Corporations.

Again the maxim 'inclusio unius est exclusio alterius' applies.

"12. On the Ground That Mutuals Are A 'Non Commercial' Enterprise.

La Societe Mutuelle brief, p. 9:

'Therefore, companies limiting their operations to their

members have no commercial character.'

It is Submitted:

(a) That this ground of exemption is difficult to understand since it turns on the words 'non commercial'.

(i) Shorter Oxford English Dictionary defines:

Commerce. Exchange between men of the products of nature and art; buying and selling together; exchange of merchandise esp. on a large scale between different countries and districts, 1587.

Commercial. 1. Engaged in commerce, trading.
2. Of or relating to commerce or trade, 1744.
3. Such as passes current in the transaction of commerce. 4. Viewed as a matter of profit and loss, 1882.

(ii) Webster's New International Dictionary, Second Edition, defines:

Commerce. Business intercourse; esp. the exchange or buying and selling of commodities and particularly the exchange of merchandise on a large scale between different places or communities; extended trade or traffic.

Commercial. 1. Of or pertaining to commerce; mercantile; hence, variously: occupied with commerce; engaged in trade; as, commercial houses; relating to or dealing with commerce; as, a commercial treaty; of the nature of commerce; as, a commercial transaction; derived by commerce or trade; as commercial profits; fit for commerce; as, commercial wares, or packages (often implying inferiority or dilution; as, commercial butter or alcohol); in respect of commerce; as, commercial success.

2. Having financial profit as the primary aim;
as, a commercial drama.

(b) That in the sense that 'non commercial' means not dealing in product and merchandise, the word applies equally to all insurers.

(c) That in the sense that 'non commercial' means non profit making this question is the nub of the divergence of views between Mutual and Joint Stock insurers that is presently before the Commission.

"13. On the Ground that Mutuals are 'At The Service of Agriculture'

La Societe Mutuelle brief, p.10:

'The agricultural class has always been favored especially by the legislator..... The companies we represent have been all instituted to render services to farmers.'

"It is Submitted:

That if any such ground is a sound ground for government policy, it does not serve as an argument for all Mutuals since only a limited number serve agriculturists in the main.

Factory Mutual brief, p. 8:

'The companies insure almost exclusively manufacturing and commercial properties of high-grade construction.'

Factory Mutual supplemental brief, p.23:

'Now, since every policyholder in the Factory Mutuals in Canada is a trading or business corporation.....'

Reciprocal brief, p.2:

'Nearly all of the subscribers are corporate bodies.'

Ontario Cash Mutual brief, p.2:

'The Four Cash-Mutuals insure at least 16,000 farm risks.'

But the combined net premiums of these four companies in 1943 was \$2,122,300. so that the farm business

would appear to be only incidental to their main operations.

The American Mutual Alliance give no information on this ground. The fact, however, is that they compete generally in the whole insurance field.

"14. On the Ground That They Are 'Small Enterprise' Based On 'Private Initiative'.

La Societe Mutuelle brief, p.11:

'The statistics hereabove quoted from the official reports of the Department of Insurance show that their average reserve fund is lower than \$1,500. and prevents any considerable extent of their operations.On the other hand, those mutuals, born of private initiative, serve public interest.'

It is Submitted:

- (a) That the admission that they are 'born of private initiative' eliminates one suggested distinction between mutuals and joint stock companies.
- (b) That if 'smallness' is a ground of tax consideration, it should apply to all enterprises based on the 'private initiative.'
- (c) That this ground has no application whatever to insurers classified as:
 - (i) Factory Mutuals
 - (ii) Reciprocal
 - (iii) Ontario Cash Mutuals
 - (iv) Members of the American Mutual Alliance
 - (v) And a large number of other mutual insurers not falling within any of the groups mentioned above.

"15. On the Ground That 'The Destination or Distribution of The Income Affected' Is a Determining Factor As To Whether a Corporation is Subject To Tax.

Factory Mutual supplementary brief, p.5:

'The ownership and control of a Factory Mutual is a policyholder's interest. Of course, the fiscal planners must discriminate in taxation of such different interests according to the destination or distribution of the income affected.'

It is Submitted:

(a) That the answer to this proposition is found in the judgment of Lord Blackburn in *Mersey Dock & Harbour Board vs. Lucas*, 1883, 8 A.C., p. 891.

(b) That the money to pay taxes of any insurer must in the last analysis come from the premium dollar. 'It requires no argument to convince any one that all items of tax upon insurance companies become a part of the general premium charge.....' (Illinois Fire Insurance Commission, 1911 - see Exhibit 'A').

(c) That if it is admitted that reserves are necessary for an insurer, reserves must for the most part be built up out of surplus earnings.

(i) 'This underwriting profit is in addition to the investment income of any other income earned by these companies in Canada of which the greater part is earned by the investments of funds contributed by policyholders. (Factory Mutual brief, p.6)

(ii) 'The major portion of the funds invested by all insurers from which this investment income is derived is moneys contributed by policyholders.'

(Factory Mutual brief, p.18)

Hence in order to secure reserves it is necessary for any insurer to make a profit and if a profit is made a tax must be paid and therefore such taxes do enter the 'premium structure'.

"Therefore, as the operating surplus of a joint stock company is affected by taxes, the cost of insurance to policy holders is reflected in the premium rate, to the disadvantage of the policy holder of a joint stock company as compared with the policy holder of a mutual insurance company which escapes its contributions to the cost of government.

"16. The 'consideration' for a policy and 'premium'.

"Finally, it has been submitted with respect to the taxation of mutuals and reciprocals (whether premium tax or income tax) that the 'consideration' of the policy is not properly called 'premium' and that the true premium is not the 'consideration' for the contract but the 'consideration' less any policy dividend paid to the assured.

(a) Factory Mutual brief, p. 8:

'That this is not a "premium" is shown by the fact that the deposit is the same amount whatever the term of the insurance.'

(b) Factory Mutual brief, p. 10:

'A fact which must be kept clearly in mind at all times is that the original deposit, which is purposely large in the case of the factory mutual companies, is a deposit and not a premium in the usual sense of the word.'

See also section V of said brief, p. 10 et seq., and section entitled 'The nature of the premium deposits,' supplementary brief, p. 10 et seq.

(c) Reciprocal brief, p. 3:

'Theoretically the amount deposited by a subscriber need be only sufficient to take care of his portion of the cost of operating the exchange.'

(d) Reciprocal brief, p. 3:

'The portion of the deposit that is returned to him is not really a dividend because it is merely the unused part of a fund previously advanced by the subscriber.

"It is submitted:

(a) That such conception of the word 'premium' is at variance with all accepted definitions, text book or statutory. 'Premium', in brief, is always defined as the 'consideration' for the contract. (See Exhibit "G" for Text Book and statutory definitions and Art. 2469 Civil Code of Lower Canada).

(b) That any quoted premium is an estimate only. (See Joint Stock Companies brief, p. 7, section 'Dividend to policy holders cannot be deductible as expense').

(i) The rates quoted by rating bureaus being an estimate only, it is not uncommon for underwriters to ask and receive premiums in excess of that promulgated by a bureau.

(ii) The excess charged in such cases over the promulgated rate does not change the nature of a 'consideration' from 'premium' to something else.

(c) That the practice of factory mutuals and reciprocals of making the 'consideration' for a contract relatively high does not of itself change the 'consideration' to something other than premium.

(i) The first purpose of any premium is to pay losses and expenses and this admittedly is the purpose of the 'consideration' exacted by both mutuals and reciprocals.

(1) 'It varies somewhat between individual properties of different classifications in accordance

with what experience has shown to be a proper measure of the difference in hazard.' (Factory Mutual brief, p. 10.

(2) 'During the life of the policy each deposit is charged each month with its pro rata share of the losses and expenses and contributions to reserves.' (Factory mutual brief, p. 9).

(3) 'The attorney (in the case of reciprocals) deducts from this amount such sum as may be required to pay losses and expenses and provide necessary reserves and surplus.' (Reciprocal brief, p. 2).

(ii) Such 'consideration' goes to make up 'income' as referred to in section 3, ss. 1, Income War Tax Act.

(Subparagraph (d) follows)

"(d) That the practice of charging the same 'consideration', irrespective of the period of the policy likewise does not change the nature of that 'consideration' to something other than 'premium'.

(1) Normally, insurance purchased for other than standard periods of one or three years, is not purchased at pro rata or an annual or triennial rate, but at a cost in excess of it; e.g., the pro rata charge for fire and automobile policies for one month would be $8\frac{1}{3}$ per cent of the annual premium. The fact is that it is the practice to charge 20 per cent (short rate table). This surcharge of nearly 150 per cent over the pro rata rate does not change the nature of the 'consideration' to something other than 'premium'.

(ii) It is common in certain classes of bonds, for example; contract, probate, insolvency, court, public administrator, succession duty and fidelity bonds, to charge the full first annual premium irrespective of what period short of this that the bond runs, i.e., underwriters say the premium is the same whether the bond is for one month or twelve months just as the factory mutuals and reciprocals say the premium is the same whether for one year or more,

'The initial premium deposit is the same for all policy terms.' (Factory Mutual brief, p. 10).

The 'consideration' for such a contract does not become something other than 'premium' because the premium is the same for one month or twelve.

"(e) That to concede the principle that dividends are deductible as expense or that the true premium is the net cost to the insured, is tantamount to accepting the

principle that is sound to permit a corporate taxpayer to first ascertain its profit and then determine what portion of it, if any, it will distribute:

- (i) as taxes to the Crown;
- (ii) as dividend or discount to its customers;
- (iii) as reserve or dividend for the benefit of its shareholders.

"(f) That if 'consideration' is not the premium, the application of statutory condition 10, R.S.O. 1937, cap. 256, sec. 106, and comparable statutory condition of the other provinces, produces an absurdity.

(i) Said statutory condition 10 reads as follows:

'The insurance may be terminated:

- (a) subject to the provisions of condition 9, by the insurer giving to the insured at any time fifteen days' notice of cancellation by registered mail, or five days' notice of cancellation personally delivered, and, if the insurance is on the cash plan, refunding the excess of premium actually paid by the insured beyond the pro rata premium for the expired time;
- (b) if on the cash plan, by the insured giving written notice of termination to the insurer, in which case the insurer shall upon surrender of this policy, refund the excess of premium actually paid by the insured beyond the customary short rate for the expired time.'

(ii) If the deposit premium mutuals, reciprocals, Canadian cash mutuals, American cash mutuals or any other type of mutual, taking a cash premium in advance is not said to be upon the cash plan or the 'consideration' for the contract is said not to be 'premium', then statutory condition 10 requires no refund upon

cancellation where the policy is cancelled mid-term by the insurer.

(iii) If it is said to be on the cash plan where a cash premium is taken in advance, sub-paragraph (b) of 10 provides, in the event of cancellation by the insured, for the refund of 'the excess of premium actually paid by the insured beyond the customary short rate for the expired time'.

If it is argued that the cash 'consideration' for the contract is not premium, then statutory condition 10 does not require the insurer to refund any part of the 'consideration'.

(iv) This is reductio ad absurdum, since:

(1) If such mutual business is said to be not on the cash plan, the insurer can cancel by fifteen days' notice and make no refund whatever of unearned premium.

(2) If it is on the cash plan but the whole of the cash consideration is not premium and an insured sees fit to cancel, the insurer need not refund short date of the total cash consideration but only short date of that portion of the cash consideration considered to be premium.

(3) Where the insurer cancels, the insured may suffer most, i.e. he gets nothing back whereas if the insured cancels he gets short date on whatever may be considered premium which is the opposite effect to that prescribed by section 10 for business on the cash plan.

Re province of Quebec - situation similar - see statutory condition 19.

(v) If the consideration is not premium, the said statutory condition has no application and an insured of a mutual company has no statutory right to a refund upon cancellation of the policy, either by himself or the insured. This fact is of more importance when the 'consideration' is said to be 8 to 20 times 'the net cost of insurance for one year'. (Factory Mutual brief, p. 8).

(g) That the Dominion Superintendent of Insurance treats the 'consideration' in mutual and reciprocal contracts in toto as premium for the purposes of his department.

(Paragraph (h) struck out)

(i) That cost of insurance and loss ratios cannot be compared when one group sets losses against net premiums for the year as required by the Dominion Superintendent of Insurance, and another group chooses an arbitrary formula of setting losses against the total deposits in hand at a specific date. In the one case, it is losses against income, in the other it is losses against assets.

(j) That appendix V of the brief of the American Mutual Alliance sets out the dividend resolutions of several members thereof, and discloses that the dividend percentage is set in advance for the various classes of risks, confirming the contention that a policy dividend is not a return of estimate over actual cost. (See Joint Stock Companies brief, p. 7, re 'Dividend to policy holders not deductible as expense').

(k) That no insurer can ever ascertain the actual cost to it of any particular risk. (See Joint Stock Companies brief, p. 7).

Part II

"With respect to the allegations made against joint stock insurers generally and certain of them particularly:

"The following allegations are made in the briefs and submissions of the various mutual and reciprocal insurers, filed before the Commission.

"1. As to the Dissemination of Misinformation and Propaganda.

(a) Factory Mutual brief, p. 3:

'Much misinformation has been given to the public, and especially to agents of joint stock insurance companies, about the present tax levies on fire insurance business.'

(b) Factory Mutual brief, p. 3:

'See also an address by Mr. A. Leslie Ham, Manager of the Canadian Underwriters' Association, Montreal, as printed in "The Chronicle" of December 11, 1942, at pages 885-887 for another example of obscurantist propaganda promoting the same misunderstanding of facts and feeding the same prejudice of ignorance.'

(c) Factory Mutual brief, p. 19:

'Those representations must mean that those people who are pressing this Commission for net taxation upon factory mutual insurers wish to have, not equal treatment of insurers, as they profess they do, but some special formula devised which will impose upon these mutual insurers some additional burden of taxation, on a principle different from and inconsistent with that applied to joint-stock companies under the Income and Excess Profits Tax Act. If so, they should now put forward their proposals for criticism, instead of relying on misinformation and meaningless slogans like "equal treatment for all" or "taxation according to ability to pay".'

(d) Factory Mutual brief, p. 27:

'The growth of these forms of mutual insurance in Canada is the occasion of the out-cry from their competitors who seek, by any available means, to stop the progress of the mutuals. That they hope to use this Commission to that end is made very clear by the circular letter addressed by the Ontario Insurance Agents' Association to its members at the time the order in council appointing this Commission was under consideration by the government.'

(e) Ontario Cash Mutual brief, p.2:

'The broad shift from reliance on premium notes, payable in arrears, to cash premiums paid in advance was brought about by the stock companies. In entering the fire insurance field the stock companies approached the public with the cry that the mutual policy holders' liability was never fixed but was undetermined and

unlimited, and that a mutual policy gave no security.'

(f) Ontario Cash Mutual brief, p. 19:

'The four Cash Mutuals and other mutual insurance companies, in order to combat the fierce propaganda which has been issued by stock companies for years, have found it absolutely necessary to conserve, to a greater degree than the stock companies, their distributable surplus.'

"It is submitted:

(a) That the allegations are completely unfounded in fact; it has been stated and is here repeated that there has been tax avoidance under any reasonable interpretation of section 4(g) of the I.W.T. Act by mutual insurers generally and that it has been shown to amount to tax evasion in at least the instance of the Joint Stock Mutuals. (See schedule "C", Joint Stock Companies brief, re 'Joint Stock Mutuals not paying taxes under the I.W.T. Act and Excess Profits Tax Act, prior to 1940 business').

(b) That in bringing this question to the attention of the public and the government, scrupulous care was taken to state facts and facts only.

(c) That the allegation that the Joint Stock Companies brief is legalistic removes that brief from the charge of dissemination of misinformation and propaganda.

"2. As to inordinate profits alleged to have been made by joint stock companies.

A. Re: Profits of British companies operating in Canada: Factory Mutual brief, p. 6:

'... that in sixty-six years, 1875 to 1940, the excess of premiums received by British companies in Canada over all losses incurred and expenses and taxes

paid was \$60,549,557.'

"It is submitted:

(a) That this reference made by the American factory mutuals against the British joint stock insurers is unfair.

(b) That the statement of sixty million dollars profit is meaningless unless it is related to some other fact. The factory mutuals stated the figure without reference to:

capital invested in such enterprises; or
the amount at risk over the years.

The British companies had at risk in Canada in the year 1940, the colossal sum of \$4,859,150,254.

(c) That accepting the figures quoted, the annual average profit for that period was \$917,417.

(d) That in 1940 there were 68 British companies operating in Canada so that the annual average profit would be \$13,491. per company if there had been that number of companies operating throughout that period.

(e) That the statement quoted is misleading to the extent that the facts are thrown out of perspective because with the same nominal average earnings per annum the gross figure can become Gargantuan by the mere effluxion of time.

B. Re: War profits made by joint stock companies in Canada:

Factory Mutual brief, p. 5:

'War conditions have greatly increased fire insurance revenues without, (fortunately for Canada) increasing the losses and expenses proportionately. Special war

risk indemnities have been sold by fire insurance companies in Canada and the United States, at rates which anticipated serious losses - losses which did not happen. The initial rate was wisely made high to cover unknown risks - but the mutuals and reciprocals gave back to their policy holders a large portion of this excess collection in their unabsorbed premium deposit return; not so the stock companies. Those high premiums produced high profits and high taxes, etc. . . .'

"It is submitted:

"That special war risks fall into two categories so far as the fire insurance business is concerned:

(a) Those falling within the scope of the War Damage Act 1942, Statutes of Canada, cap. 35.

This is a government insurance fund. Fire insurers generally assisted in the organization of and do assist in the operation of the fund under administrator and an advisory committee made up of representatives of the several classes of insurers and government officials.

Section 26 provides that the minister may enter into an agreement with any insurance company with respect to the remuneration to the company for the functions fulfilled under the act.

Explanatory notes and instructions of the war risk insurance scheme - section 23 provides the term of remuneration to companies 2-1/2 per cent of the premium with a minimum of 50 cents and a maximum of \$250 per policy.

Section 21 of said explanatory notes and instructions provides remuneration for agents of companies, 5 per cent of the premium, with a minimum of 75 cents and a maximum of \$500.

Section 20 of said explanatory notes and instructions, defines agent as 'any fire insurance agent duly licensed by a province of Canada as such,' and further provides: 'A direct writing mutual company or reciprocal exchange duly registered with the Dominion Government may also act as agent.'

Therefore, joint stock companies were limited in remuneration to that set forth above, i.e. 2-1/2 per cent. Deposit premium mutuals and reciprocals are entitled to receive both remuneration as a company and as an agent, i.e. 7-1/2 per cent or 300 per cent of that of the joint stock companies.

(b) Cover granted by special endorsements known in the business as war risk endorsements 1 and 2, which were developed to 'bridge the gap' between the cover granted by a standard fire policy with supplemental contract and the cover obtainable under the War Damage Act.

In view of the fact that the records of the Canadian Underwriters' Association covering the operations of 167 member companies disclose that the members in toto in neither the years 1943 or 1944 wrote more than \$50,000 to \$60,000 in premiums for these endorsements, it can hardly be said that this special war risk endorsement has added so much to the companies' profits.

(c) If the reference is made to insurance business arising out of the industrial development caused by the war, it should be pointed out that such risks are rated on the same schedules as are used in peacetime for such industries. Special war risks for which such industries might seek cover must be sought under the War Damage Act or the two special endorsements dealt with above.

"C. Re: High rate of profit apart from special war risk.

(a) Factory Mutual brief, p. 6:

'Of course, war conditions merely underlined and exaggerated pre-war conditions in respect of fire insurance profits both in Canada and the United States.'

(b) Factory Mutual brief, p. 26:

'But the major consideration, which creates the crisis in the fire insurance field is the high rate of profit which joint stock fire insurance companies have been making consistently over a long period of years on their Canadian business.'

(c) Factory Mutual supplementary submission, p.14:

'Assuming, as we reasonably may, substantially all this business, excluding the factory mutuals, is written at tariff-bureau rates, it would seem that joint stock companies' rate-differentials for classes of risk are not beyond criticism, and that such a rate was too high a price to pay for fixed-premium insurance of the best protected class of Canadian risk.'

(d) Reciprocal brief, p. 7:

'The very favourable loss experience and the high earnings of stock companies in Canada show how immune the premium rate regulating procedure of those companies is to consideration of interest to the policy holders.'

"Set out hereunder is a statement of the profits made in the fire insurance business from 1875 to 1940:

Period	Canadian Companies	British Companies	Foreign Companies	All Companies
		%	%	%
1869-78	-15.01	-17.56	- 2.28	- 12.29
1879-88	- 2.13	10.20	16.59	7.59
1889-98	0.52	3.84	0.85	2.65
1899-08	- 1.65	5.43	9.06	4.62
1909-18	2.88	9.65	7.26	7.68
1919-28	1.65	5.60	4.71	4.70
1929-38	8.11	6.04	6.28	6.52
for 70 years. .	<u>2.74</u>	<u>6.01</u>	<u>5.83</u>	<u>5.37</u>
1939	11.50	13.22	12.59	12.57
1940	14.11	13.27	13.90	13.72
1941	9.25	4.47	6.19	6.30
1942	5.74	5.78	8.05	6.52
1943	10.28	2.46	5.53	5.64

Quoted from the Report of the Dominion Superintendent of Insurance for business of 1943 - page L.

The following figures show that while insurance premiums in 1944 have increased over 1939 by 33.9%, the losses in that period have increased by 37%.

Year	Net Premiums Written	% increase over 1939	Net Losses incurred	Loss Ratio	% increase over 1939 or reduction from 1939
1939	\$40,984,276.	-	\$15,738,902.	38.4	-
1940	41,922,312.	2.3	15,444,927.	36.8	-4.2
1941	49,305,539.	20.3	17,814,322.	36.1	-6.0
1942	47,272,440.	15.3	20,360,534.	43.1	+12.2
1943	47,153,094.	15.1	22,181,244.	47.0	+22.4
*1944	54,902,183.	33.9	28,869,700.	52.6	+37.0

Extracts from Table I of the Report of the Superintendent of Insurance of the Dominion of Canada for the years indicated.

*Obtained from the Superintendents' Memorandum re Advance Insurance figures, Table I.

"It is Submitted:

(a) That the following is a false doctrine: 'Insurance shareholders' profits always depend on higher premiums.' (Factory Mutual supplementary brief, p. 21). Not only does the law of diminishing return hold true in the insurance business, but it has a peculiar effect with respect to insurance. To insure one risk is a bet or a gamble; to insure many risks is a business. Price affects the size of the market and the market determines the opportunity to secure spread of risks. This fact is known to every underwriter. The above allegation can only mean that the joint stock insurers are charged with being ignorant of this fact, or this fact is ignored by the authors of the factory mutual brief in order that the allegation might be made.

(b) That the statement: 'In recent years the amount of taxes paid by individual companies with share capital has been high because the profits have been unusually high.' (Reciprocal brief, p. 6), completely ignores the fact that taxes may be higher because a war is in progress and tax rates have been raised in recent years to pay the cost of the war.

(c) That the statement: 'but the economic value of the competition afforded by exchanges and also by mutuals is of great importance' (Reciprocal brief, p. 5), can be accepted or rejected but in either case the importance is not such as to justify the subsidizing of mutuals and reciprocals out of the purse of their competitors.

3. "As to the Cost to the Public of the Agency System"

(a) Factory Mutual brief, p. 26:

"In the next place, the discrepancy between the cost of operation of the joint-stock fire insurance business and that of the purely mutual fire companies operating on the premium deposit plan, without commission paid agents, is greater than..."

(b) Factory Mutual supplementary brief, p. 22:

"It is otherwise with the factory mutuals, in which the policyholder has always the full advantage of reduced costs resulting from reduced hazard and where no commission paid agents earn an advantage from high rates of commission and high rates of premium."

"It is Submitted:

(a) That this is one point where there will be no unanimity in the pleas of mutuals or in the minds of the insurance buying public.

(b) That the factory mutuals and reciprocals may deprecate the value of the agency system, but the Ontario cash mutuals and the members of the American Mutual Alliance will not be heard to say anything against it since they, like joint stock insurers, avail themselves of it and it is an integral part of their system of operation.

(c) That the insurance buying public in Canada seems to find a value in the agency system since 96.7% of the fire business in 1943 was written by insurers other than the factory mutuals and reciprocals.

'There is no doubt of the value and importance of the agent to the fire insurance business, and taking all things into consideration the agency system appears at the present time to be best suited to the needs of our people of Ontario.' (Ontario Insurance'

Commission, 1916-1918 - p. 18).

4. "As to Competition and the Lack of it

(a) As between tariff companies and others:

Some joint stock insurers are members of what is called underwriters' associations; on the other hand, some are not. In Ontario and Quebec there are the following competitors.

Licensed insurers transacting business falling within the classes controlled by the Canadian Underwriters' Association.

<u>* Ontario</u>		<u>** Quebec</u>	
Farmers' Mutuels	67	County Mutuels	9
Cash Mutuels	12	Municipal Mutuels	77
Factory Mutuels	11	Parish Mutuels	234
Other Mutuels	14	Factory Mutuels	11
Reciprocal Exchanges	11	Other Mutuels	26
Non-tariff stock Cos.	70	Reciproicals	9
	—	Non-tariff stock Cos.	74
Total non-tariff Cos. excluding Lloyds Underwriters	<u>185</u>	Total non-tariff Cos. excluding Lloyds Underwriters	<u>440</u>
Tariff companies	163	Tariff companies	166

* Source: 1943 Report of the Superintendent of Insurance for the Province of Ontario.

** Source: 1944 Report of the Superintendent of Insurance for the Province of Quebec.

It is submitted that the 160 odd tariff companies or the 230 odd joint stock companies have ample competition as disclosed by the above figures.

(b) As between Joint Stock Insurers themselves

The members of a tariff association not only compete with joint stock and mutual insurers not members, but compete most strenuously amongst them-

selves under the urge no doubt of the 'profit motive'. It would be too much to believe that this motive would be so strong as to be responsible for all the evils alleged against the 'profit motive' by the Mutuals and Reciprocals, and at the same time be so amenable as to eliminate competition between the members of a voluntary association of competitors. The 'profit motive' is such that any member of an association who can by surveying and servicing a risk secure a rate reduction for an assured and the business for itself, never stops to question what type of an insurer it has been able to outdo.

(c) As between certain Joint Stock Insurers and Mutuals

(i) There is a manifest tendency on the part of the stock companies grouped in rating bureaus such as the Canadian Underwriters' Association to make competition with them difficult. (Reciprocal brief, p. 10).

With respect to this allegation, it needs only be observed that competition that is not difficult hardly deserves the name of competition.

(ii) There are several allegations of monopolistic tendencies of certain joint stock companies.

'They (Ontario Cash Mutuals) have served the insuring public in Canada efficiently against the monopolistic tendencies of the stock companies, exercised through Canadian Underwriters' Association....'

It is to be noted first that one or more of the Ontario cash mutuals are members of the Independent Fire Insurance Conference and the

Independent Automobile Conference, both of which conferences have joint stock companies and mutuals in their membership. These conferences function similarly to the underwriters' associations with respect to rating problems and other matters of common interest to the members and do so in the interest of the business. But why such activities should be considered monopolistic when carried on by joint stock insurers alone but not when carried on by mutual insurers is difficult to understand.

It is likewise to be noted that the factory mutuals collaborate, the reciprocals collaborate and members of the American Mutual Alliance collaborate. Is such collaboration in itself only monopolistic when done by one's competitors?

The allegation of monopoly or monopolistic tendency must have been made with no reference to the meanings of those words.

Shorter Oxford English Dictionary defines:

Monopoly. Exclusive possession of the trade in some community and exclusive privilege of selling some commodity or trading with a particular place or country; exclusive possession, control or exercising of something.

It is suggested that the allegation of 'monopoly' is incompatible with the allegation of 'fierce competition' in the business and the figures quoted above belie the charge. The members of the Canadian Underwriters' Association write approximately half of the fire business in Ontario and Quebec and they do it in competition with a vast number of competitors as shown above.

"5. Sundry other allegations none of which are at issue or pertinent to this inquiry.

(a) Re: Underwriters' plans and rating material.

(i) These are produced by underwriters' associations for the use of their members and the use of their agents. 'Incidentally the system of schedule rating tends to the reduction of the fire waste of the country, and the governing body of the association have as individuals probably become more deeply interested in the reduction of fire waste in the province than any person outside the Fire Marshal's office.' (Ontario Insurance Commission, 1916-1918 - p. 7).

(ii) Their competitors are free to do likewise either individually or as a group. In fact, the Independent Fire Insurance Conference, of which some if not all of the cash mutuals belong, are developing rating schedules and securing plans from independent contractors.

It has never been suggested that the engineering plans and rates spoken so highly of by the factory mutuals and reciprocals, as their contribution to the public welfare, should be made available to the joint stock insurers generally for the purposes of competition. (See Underwriters' Survey Bureau Ltd. Ltd. et al, vs. Massie & Renwick Ltd., 1938, Ex. C.R. 103, and the appeal 1944, S.C.R. 218).

(b) Re: Agency Registration Plan:

This plan is only a method designed to secure the agents of member companies against the unfair competition of their agency competitors by restricting the distribution of plans and rating material to agents who use the information to secure business for themselves and their

principals who have not supplied them with such facilities. (See Underwriters' Survey Bureau Ltd. and Canadian Underwriters' Association vs. Haig, McDougall & Bateman Ltd., 12 I.L.R. 1945, p. 15).

(c) Re: Fleet operation of companies:

There are, it is true, companies that are operated in fleets or groups. Such companies in a group may be owned:

(i) by one member of the group;

(ii) in part by one member of the group, other shares being held by other shareholders, in which case the control of the companies may rest with the parent company or with the other shareholders;

(iii) by shareholders other than a company in the group, but placed with other companies under common management.

This condition may exist for a multitude of reasons, one of the more dominant reasons being one of the economy in administration; other reasons are with respect to re-insurance facilities or the continuance of an agency connection built up by the purchased company and purchased as part of the goodwill at the time that the acquisition was made.

"With respect to the allegations dealt with under this paragraph 5, it is submitted that they are impertinent to the reference, and are alleged not as a point upon which the question of liability to tax of mutuals and reciprocals can turn, but rather to becloud that issue with extraneous references.

"Finally it is submitted:

"1. That mutuals generally are taxable, and have always been taxable under the War Income Tax Act and the Excess Profits Tax Act since their method of operation does not

bring them within the exemption afforded by section 4(g) of the I.W.T. Act.

"2. That none of the grounds alleged as reasons for exemption warrant a decision that they should be exempt.

"3. That it is not in the public interest nor should it be public policy that the tax discrimination presently existing should continue.

Montreal, 16th April, 1945.

Aime Geoffrion, K.C.
Counsel.

J. A. Mann, K.C.
A. Leslie Ham,

For the Joint Stock
Companies."

(Page 6325 follows)

A. LESLIE HAM,

Manager, Canadian Under-
writers Association,
Montreal, P.Q.,
having been duly sworn,
testified as follows:

BY MR. MANN:

Q. Mr. Ham, you are manager of the Canadian Underwriters Association? A. Yes, sir.

Q. Residing in Montreal? A. Yes, sir.

Q. Did you, in collaboration with counsel, prepare a brief which is dated February 3, 1945, and a supplementary brief dated April 16, 1945, for the information, use and assistance of this Commission, relative to the inquiry which is now being conducted? A. I did.

Q. To your belief are the statements of fact made in these documents to which I refer true? A. Yes, sir.

Q. And in so far as they relate to information received, statistics garnered, and matters of that kind, do you believe them to be true? A. I believe them to be true.

Q. You have copies of the briefs in front of you, have you? A. Yes, sir.

Q. There are one or two matters on which I want to enlarge, and I will be very short. During the proceedings before this Commission a statement was made, I think the day before yesterday, that the ratio of mutual business to stock business was not more than 10 per cent, and probably 8 per cent. Can you make any statement with reference to that? A. Well, I had compiled figures from the Blue Book which disclose --

MR. PARKER: Who made that statement?

MR. MANN: Mr. Mason.

MR. HAYDEN: The brief states that the figure was 87.5 per cent in 1942.

THE WITNESS: It is in the record.

BY MR. MANN:

Q. Is it in the record? A. The statement that it was not exceeding 10 per cent, and was more likely $8\frac{1}{2}$ per cent.

Q. That does not make the stock companies 87.5 per cent?

MR. ELLIOTT: As I recollect it, Mr. Mason corrected the original figure.

MR. MANN: I am very sorry I did not appreciate that.

MR. MASON: That was not worrying me.

MR. MANN: We will not have to deal with that, then.

Q. Now, in respect to the mutual insurers, relative to losses incurred in Canada as compared to losses charged to Canada -- do you understand what I mean? A. That is with respect to the factory mutuals?

Q. Yes. Have you any statement to make with reference to that? A. I have compiled the figures for the factory mutuals Canadian business, 1936 to 1943 inclusive. From the Blue Book the net premiums written were \$4,893,155. The net losses incurred were \$1,194,026. From Best's insurance reports, applying the 7 per cent formula mentioned in the brief to their total losses as disclosed there, there would be chargeable to Canada \$1,578,586; or the Canadian business bore the sum of \$384,560 more than the actual losses incurred in Canada. Of course that is based on the 7 per cent formula, as set out in Mr. Gray's brief.

Q. The ratio as taken by Mr. Gray did not reflect the actual losses in Canada? A. That is so.

Q. And what you are giving are the actual losses that did occur in Canada? A. Yes.

Q. With regard to the Ontario Cash Mutuals, may I draw your attention to page 4 of their brief, the second paragraph from the top of the page, which reads as follows:

"With the stock companies it is desirable to maintain as high rates as competition will permit and to select only the choicest risks, so that dividends will be as great as possible. In contrast in the case of the mutuals, there is no such conflict. The whole reason of their existence is protection, and in consequence there is no motive to maintain higher premium rates than necessary to provide that protection from day to day, with adequate reserves to meet contingent unusual underwriting losses."

Is there anything you would like to say with respect to the operations of the stock companies in regard to the inference to be drawn from the words used in that paragraph?

A. I would suggest that using the practice of schedule-rating, as it is used in the fire insurance business, is incompatible with the suggestion that joint stock companies derive their biggest benefit from maintaining as high rates as possible. Furthermore, the fact is that to an insurer the spread of risk is just as important as any other factor in order to get his law of averages working. Therefore disproportionately high rates curtail his market and his chance of obtaining the spread of the risk. The application of schedule-rating as to risks tends to eliminate discrimination and to have the insured himself make the rate applicable to the risk, by whatever improvements he will make on it. Or if he is content to have the risk sub-standard, he will have to pay a penalty for sub-standard conditions.

Q. By "sub-standard conditions" I take it you mean unusually hazardous risks? A. Yes. We work from a standard. An assured may have a better than standard risk or worse than standard. If he has a better than standard risk he gets credit under the schedule. If it is worse than standard, he pays a penalty.

Q. I notice Mr. Robertson does not say that the stock companies select only the choicest risks, but he does say that in the stock companies it is desirable to maintain as high rates as competition will permit, and to select only the choicest risks. As a matter of fact the stock companies do what, in respect of general insurance? A. The stock companies generally write the general run of business across Canada. Each underwriter, as was stated the other day, in accepting and rejecting risks makes a choice, and hopes that his judgment is sound. He does not take on a bad risk just because it is bad; but the joint stock companies service the whole of Canada's commerce, from lumber in the bush, which is considered by many to be a bad risk, up to the very high-class risks that Mr. Gray's brief deals with.

Q. In which Mr. Gray's plant indulge exclusively?

A. They are sprinklered risks and fireproof protection.

Q. What about farm underwriting? A. Farm risks are readily accepted by a number of companies. Other companies do not like them as a class; but the joint stock companies are definitely in the farm risk business and write a considerable proportion of it across Canada.

Q. Would you suggest that the joint stock companies, as far as the writing of farm risks is concerned, which I think you heard them explain some of the farm mutuals are unable to write, are a benefit to the farm insuring public?

A. To the extent that insurance is available to the farmer from the joint stock companies, it is a benefit.

Q. And it is available to the farmer? A. It is available to the public.

Q. I am not talking about half a dozen companies, or eight or ten companies; I am talking generally about the stock companies, for which you are speaking to-day. A. Yes, generally from the stock companies.

MR. MANN: That is all, thank you.

BY MR. PARKER:

Q. Well, Mr. Ham, I will not be met by the statement from you that you are not a lawyer, will I? A. No, sir.

Q. In reference to that last point it is true, is it not, that the farm mutuals particularly render a great deal wider service to the farm risks than do the ordinary joint stock companies? There is no question about that? A. I would think there is no doubt that the farm mutuals serve a bigger portion of the farming community than the joint stock companies.

Q. Not only bigger, but very much bigger? A. Yes. There is no question about that.

Q. And you would agree that the briefs dealing with them were not a bit exaggerated, in the way they were put up?

A. Quite.

Q. You say that you take responsibility, in a sense, for the statements alleged in the briefs. You are familiar with them; you helped prepare them? A. Yes, I did.

Q. And you vouch for them? A. Yes, sir.

Q. I understand that the All Canada Federation is merely an advisory body? A. That is true.

BY THE CHAIRMAN:

Q. If I may interject a question, Mr. Ham, do you think that the stock companies would furnish and could furnish adequate protection of the farming communities? A. When you say "could" I would have to say yes, that it could be done.

Q. Do they do it? A. The facilities are there. In my own mind there is no question that the farm mutuals fulfill a very useful function in the community.

BY MR. PARKER:

Q. That is theoretical; they could render full service, but practically they do not? A. Yes. The fact is that they fulfill an important service.

BY MR. ARNASON:

Q. I understand the view of your group, Mr. Ham, is that you have no objection to the exemption of strictly farm mutuals which operate on the genuine, non-profit basis?

A. Quite so, sir.

Q. I understand that to be your view? A. Yes, sir.

Q. Suppose we have a farm mutual serving a small group of farmers within a definite area, shall we say in a rural parish in Quebec. Suppose the operations of that mutual were extended to another low income group in that area, say workmen living in a village or a town. Do you think there would be any objection, from your point of view, to the extension of this same principle to another low income group, such as workers, under the conditions which I have mentioned, assuming that the method of operation is exactly the same? A. The difficulty I foresee there is how you would establish your category and describe the other low income group. That is a difficulty in answering your question. I do not think it is a question so much, to my mind, as to farmers as a group

having mutual insurance; I do not think that has any bearing on it. It is farming as a business; and those local mutuals, because of the fact that they are in outlying communities, the mutual company knows its own insured, and it does render a peculiar service there.

BY THE CHAIRMAN:

Q. It is the condition of the risk? A. Yes.

BY MR. ARNASON:

Q. Yes, but it is conceivable, though, is it not, that you might have a group who would be interested in securing protection at the lowest possible cost and who might think that by combining their efforts with the farm group they might achieve their objective? I do not want to prolong this discussion, but I would like to get your views? A. I would see no difficulty of any group, whether it was a low income group or a high income group, if they formed the mutual company and followed the strict principles of mutuality so there was no income -- I would see no objection to it at all. Any group could do that, irrespective of the size of their income.

BY MR. NADEAU:

Q. Do any of your companies reinsure risks taken by mutual farm fire insurance people? A. That depends on the capacity in which I am speaking. The answer to that question is yes, because the joint stock companies fall into two groups, those that are known as tariff companies and the non-tariff companies. The non-tariff companies I presume, from the testimony yesterday, do exchange re-insurance with, for instance, the Ontario Cash Mutuals. That was the tenor of the evidence yesterday. The tariff companies do not exchange re-insurance except within themselves, or by treaty re-insurance

with outside companies.

The reason for that is that having taken business at a rate which we consider is a non-discriminatory rate, they could hardly accept by way of re-insurance other risks at a lower rate that was discriminatory. That is the underlying reason for the refusal to accept re-insurance from people other than members of the association.

BY MR. MANN:

Q. Perhaps my learned friend will not mind if I ask one question. When you speak of tariff companies, do you mean board companies who adhere to the tariff rates and such of the non-board companies who also adhere to the tariff rates; or do you merely mean the 167 board members? A. The 167 board members.

Q. They are board companies, then, because there are non-board companies who do adhere to the tariff rates?

A. Just because they think their judgment and ours happen to coincide.

Q. I am not interested in the reason. That condition exists? A. True. Pure coincidence.

BY MR. VAUGHAN:

Q. You said there was no objection to farm mutuals. By that do you mean there is no objection to the exemption of the farm mutuals? A. No, because they operate very closely to the principles of true mutuality. Where they do take a premium in advance perhaps they do have income. My own judgment is that they do, but where they have restricted themselves to serving a social function in the community, that almost bespeaks their mutuality.

BY THE CHAIRMAN:

Q. It gets down to this; they come nearer to the ideal

of no profit than any others?
correct.

A. That is quite

BY MR. VAUGHAN:

Q. Then we understand that the organization you represent have no objection to the exemption granted the farm mutuals?

A. As long as the conditions remain as they are now.

Q. That is not quite what is stated in paragraph (a) of your recommendations, where you say that all exemptions should be lifted except in the case of life companies? A. This is my view of it. If sections 4(i) and 4(g) of the Income War Tax Act were eliminated, the test would then depend upon whether in fact they had income and whether it inured to the benefit of their members. I think a number of the small farm mutuals would be out, on the ground that they had not any income.

BY THE CHAIRMAN:

Q. They do not need the exemptions in section 4, then?

A. No, they do not need them.

MR. VAUGHAN: I am glad you explained that, because otherwise I might have taken a different meaning from paragraph (a) of your recommendations.

BY MR. ARNASON:

Q. You say it does not necessarily follow, then, that there is any discrepancy, as it were, between mutuality and the size of the organization, as long as strict mutuality is observed? A. Quite. If strict mutuality is observed, I have no objection as to size.

BY MR. VAUGHAN:

Q. That perhaps raises the bigger question, of what is strict mutuality. However, I do not want to ask about that now.

BY MR. PARKER:

Q. Mr. Ham, I was going to ask you about the All Canada Federation. That, I understand, is not an incorporated body?

A. It is not; and I speak not as a member or officer of it, but as a fact I know that to be so.

Q. It is just an association? A. Yes, sir. It has been called an amorphous mass.

MR. MANN: Somebody said it was an amorphous mess.

BY MR. PARKER:

Q. I say it is merely a conferring body? A. Yes, sir.

Q. It has no authority to command or give directions to anybody. The Canadian Underwriters Association is an incorporated body? A. Under Part II of the Companies Act.

Q. And it is one of those who make up the group known as the All Canada Conference? A. No, sir.

Q. What makes up the All Canada Conference? A. Individual companies themselves are members, and may be members of both.

Q. Are all the members of the Canadian Underwriters Association also members of the All Canada Conference?

A. That is correct, I think.

Q. And you are representing here to-day in this brief all the members of the All Canada Conference? A. No, not all.

Q. How many? A. The 227 joint stock company members.

Q. Is that all of the joint stock company members?

A. That is all the joint stock company members --

Q. Of that conference? A. Yes, with the one exception that I know of; that is the pool insurance company, which claims exemption by virtue of being owned by a co-operative.

Q. That really has nothing to do with whether or not

it is a member of the All Canada Conference? A. In that capacity I am not acting for them, because as you see there is a conflict of interest.

Q. How did you get your instructions to act from all these companies? A. From a committee appointed representing 88 companies.

Q. Eighty-eight out of how many? A. Out of 227.

Q. Do you represent the remainder? A. The remainder have been supplied with copies of the briefs; they were filed, and they have had them in their possession.

Q. Have they affirmatively instructed you to make representations on their behalf, or have you just assumed authority to do so because they did not tell you not to? A. No, there were no individual instructions from the whole of the 227. There were instructions from the 88 companies, and they were a committee appointed by the 227 companies.

Q. And the Canadian Underwriters Association instructed you by resolution, I assume? A. I am not appearing on behalf of -- I am not here as a witness on behalf of the Canadian Underwriters Association.

Q. Are the Canadian Underwriters Association represented by the brief at all? A. No. It is the individual companies. It is the association as such.

Q. I understand that; but I understood from Mr. Mann's opening remarks that he was defending at some considerable length and with some fervour the Canadian Underwriters Association. But he is not representing them here to-day, and you are not? A. No.

Q. In the All Canada Conference, are the members all Canadian companies, or do they include British and foreign? A. British, foreign and Canadian.

Q. Does the same thing apply to the Canadian Underwriters Association? A. That is correct.

Q. And in your representations in your brief you make no distinction between the so-called Canadian companies on the one hand and the British and foreign on the other hand?

A. That is correct.

Q. You treat them all alike, and offer the same criticisms and so on of the mutuals? A. That is correct, sir.

Q. Just one or two statements in your brief; I am not going to detain you very long. We will start on page 1. This is by way of introducing yourselves:

"We have not explored the field of co-operative farm and industrial organizations, except in so far as the principles governing their operations relate or are similar to mutual and so-called mutual organizations."

What do you mean by "the principles governing their operations" relating to mutual organizations"? Just what do you mean by that? What are you trying to say there?

A. Both co-operatives and mutuals in their contention for exemption --

Q. Co-operative and mutual what? A. A mutual insurance company and a co-operative, whether it is a producer or consumer co-operative -- they base their argument --

Q. Their argument on what? A. On the exemption; that they have no income subject to tax. So to that extent they are, on the same ground in claiming the exemption.

Q. That is on the ground of mutuality, as you understand it? A. That is one of the grounds alleged by both co-operatives and mutuals.

Q. Speaking generally, they have no income because of

their -- ? A. Mutual nature.

Q. That is what you understand the argument to be?

A. Yes.

Q. And you have followed it pretty well across the country? A. Yes.

Q. That is what you say it is, in a word? A. Yes.

Q. Then you go on to the next paragraph, which will bring me to the question Commissioner Vaughan was suggesting a moment ago:

"We believe that to a material extent the terms 'cooperative,' 'reciprocal' and 'mutual' are interchangeable in respect of merchandising operations --"

Did you give that careful consideration? Do you make no distinction between cooperatives, reciprocals and mutuals, especially in relation to the insurance discussions you have heard here during this week? Do you say there is no difference between "reciprocal" and "mutual," that they can be used interchangeably? A. The difference --

Q. Would you say that? A. There is a difference in the application of the words but not in the words themselves.

Q. You do not wish to modify the statement, in view of what you have heard this week? A. No.

Q. Will you let it stand? A. Yes.

Q. Are those terms interchangeable in respect to insurance operations? A. Well, with the amendment of the Saskatchewan Insurance Act, I think it is part XI(a) by which a cooperative insurer can be organized, I can see no distinction. The three terms are now used in the insurance business.

Q. Let us go on, then:

-- but these words have been, and are being progressively

used in the description of organizations which have no relation in their operations to strict mutuality or co-operation."

What do you mean by "strict mutuality"? Take your time and tell us what you mean by those words. I am not trying to make anything difficult; I am serious about this. Perhaps before you start I should put it in this way. If a business, whether it be a trading concern or insurance company, carries on its operations in a way that can be said to be strictly mutual, then you are agreed that there is no tax payable? A. Quite.

Q. So if we can come to an understanding all round as to what that "strict mutuality" is, we will have gone a long way toward solving a lot of our difficulties, will we not? A. I quite agree.

Q. With that in mind, then, I am putting this to you: if you can tell us what are the attributes of a mutual society or organization; what must it possess? A. If you will turn to the top of page 2 I think you will find that a definition has been attempted there, in the paragraph at the top of the page:

"A, B and C agree among themselves that all will insure each, and for expenses of operation and upon the happening of a loss, each will contribute upon assessment. In such case there is no taxable income."

I suggest that would be a true mutual.

Q. You say that is a sample, but that is scarcely a definition. There may be an unlimited number of other illustrations. I am struggling for something all-inclusive, some test that we can apply. Could you help us on that?

A. If it is an organization that does not have income; that

paragraph attempts to illustrate how it could operate without income in the accepted sense of the word. There is a type of business in the insurance field, which happens to be in the life field, that would illustrate it as another example.

Q. I do not like definitions by way of examples; I do not think they are very helpful. A. Then I will say where it has no income.

Q. That is rather uncertain; that is not a definition. We do not need a definition if we can find out whether the thing has an income or not; we do not care whether it is mutual or not.

MR. HAYDEN: Even a stock company without income would not have to pay.

THE WITNESS: Well, of course, Mr. Parker, definitions are one of the most difficult things to handle.

BY MR. PARKER:

Q. I realize that. A. You cannot define it offhand.

Q. You are putting it to us on this ground; that if a company complies with strict mutuality you have no criticism to offer? A. Yes.

Q. If it does not, you think it should pay taxes. Surely, then, you have some suggestion to make as to how the Commission ^{could} draw the line? A. Applying this rule to the insurance business, I suggest that, I think, in paragraph 1; not dealing with merchandising, but with respect to the insurance business.

Q. I do not want to prolong this, but may I put it to you in this way. In the case of the reciprocals, as they were described here the other day, as I understand it there are a number of people who set out to insure each other. If

they put up sufficient money, or assume an obligation to share each other's risks if, as and when something happens, without having it complicated by having investment income, without having investments with which they have to deal; as long as they keep within themselves, is that to be considered a purely mutual operation? A. There are conditions under which it could be, but I do not think it is under the conditions that exist.

Q. Under the conditions I have just specified. What I am trying to say is, leave out the investment income; say they can keep everything within themselves. Would that be a company, within your idea as to what strict mutuality is? A. I am inclined to agree with you.

Q. Then if instead of putting up the money themselves they have to go to the public or to the investors; if they have to go into the third party atmosphere, if you like, is that the thing that takes them out of the classification of being strictly mutuals? Is that where you draw your distinction? A. Perhaps I have to take a little different ground than you suggest. The reciprocal subscriber, on entering into the contract, deducts the premium as expense, and is allowed to do so, from his own income tax returns. That is deductible as expense, as a premium. If on the other hand he were doing what they purport to do, and were a self-insurer, without the interjection of a reciprocal between himself and his money --

Q. Without the interjection of what? A. Of a reciprocal, an attorney-in-fact in the process, he would be able to set up his own self-insurance fund, but only after he had ascertained his profit and had been taxed on it, and he takes the amount of money for his self-insurance fund out

and sets it up as a reserve. But as we find it now, a subscriber deducts -- if I may use a figure -- \$10,000, either as a premium or to be set up as a self-insurance fund. If he puts it into a self-insurance fund he will have paid the tax before taking it out, it being part of his surplus and being taxable. When that \$10,000 earns income, as such, it reflects in his surplus, and he is taxable on it.

Now we take the case of a subscriber to a reciprocal. He takes his \$10,000 and deducts it as expense and credits back anything that comes back to him out of it --

Q. I did not ask you to describe in detail the whole operation. We had that yesterday. I merely asked you: if we could eliminate the investment income aspect of it; supposing they get along without depending upon investment income, and simply put up their deposits in their vault, and when a loss came they paid it? A. The attorney-in-fact paid it?

Q. Yes, but merely as an employee. A. As the agent of the group.

Q. As the employee, I suggest, rather than an agent; or in whatever capacity he is acting under that agreement?

A. Whether he acted as an employee or as an agent, I suggest that under those circumstances it is quite probable there is no income.

Q. I would think so. Therefore does it not come to this. The fact that members or subscribers, through their attorney, have to go out and invest that money, and do go out and invest it, in your submission means that they are then departing from strict mutuality? A. Yes, quite.

Q. And that takes the cloak off them, so to speak, and makes them carry on business? A. Yes.

Q. That it interjects or brings into play a sort of third party. Is that your idea? A. That is correct.

Q. Supposing I put it to you this way. Supposing all of us in this room at this moment solemnly agree that from this moment forward, and for the next year, if any one of us had a loss by fire we would all chip in and make it up, share and share alike. We do not put up anything now; we do not promise to put up anything more than that. We do not have any investment income, any power of attorney or anything; just a memorandum to which we all agree. Would that be a good illustration of a pure mutual? A. I would agree that that would be a pure mutual.

Q. Perhaps that would be the simplest type we could have? A. Yes.

Q. After consideration do you say that if you superimposed upon that simple scheme, to make sure that you and you and you would not be bankrupt when it comes time to collect on your share, that we put something up in the hands of somebody, just to hold the money to make sure we will have it when the loss comes -- do you think that would take it out of the field? Supposing we appoint one of ourselves to hold the pot? A. Then it becomes reciprocal.

Q. I do not care what it becomes.. I am asking you if it becomes non-mutual by doing that? A. No, it does not become non-mutual, because it becomes reciprocal.

Q. Then comes the third step. Instead of keeping that money among ourselves, appointing one of ourselves to represent us all, we say, "Now, like the good steward, we must not let that money lie there idle. We had better go and invest it somewhere so it will earn something." Does that take it out? A. I say it does. It creates income.

MR. VAUGHAN: Supposing those members put up bonds as security. Would that change your idea at all?

BY MR. PARKER:

Q. Yes; supposing we all put bearer bonds in the hands of one of the lot? A. And the man himself, instead of clipping his own coupons, has them clipped for him. That is still mutual.

BY MR. ARNASON:

Q. I understand you to say that investment income would tend to affect the mutuality of the group? A. Yes; that is right.

Q. In view of your previous suggestions with regard to farm mutuals, would you say that if they had some surplus funds on hand which they deposited in a savings account in a bank, just bearing in mind the fact that the membership is confined to farmers; they are farm mutuals -- would you say that the income from that savings deposit would tend to destroy the mutuality? A. To be consistent I would say yes; but I suggested that the farm organizations can be taken care of as such without relation to the principle which we are discussing. But as a group it might be good government policy --

Q. They really represent a problem by themselves?

A. Yes, I would say that, sir.

BY MR. PARKER:

Q. Then will you turn to page 3 of your brief. This apparently deals in a way with a matter on which I attempted to put a question to one of the witnesses yesterday, I think:

"We suggest it is possible that a mutual insurer having accumulated large assets and reserves might adopt an underwriting policy of its business so that eventually the board of directors alone would be the sole policy holders or

members."

You will remember that yesterday I put that question in substance to one of the witnesses, and in effect his reply, as I understood it, was that theoretically that might be possible but it was so impracticable as to be almost silly. I think that was the effect of his answer. I suggest that he made a very proper answer to my question yesterday; that theoretically that situation might come about, but that in the field of practical business such a suggestion is just silly. What do you say about that? Do you not agree?

A. I do not agree with that, sir.

Q. Is it not quite beyond the realm, almost certainly beyond the realm of probability and barely in the realm of possibility? A. Not if you can believe what you read in the newspapers.

Q. Well, you cannot, so you can skip that. A. An attempt to do that has actually occurred in Des Moines, Iowa, by the managing secretary of a mutual company.

BY MR. HAYDEN:

Q. What company? A. The American Farmers Mutual Automobile Insurance Company of Des Moines.

BY MR. PARKER:

Q. What are you reading from now? A. The Journal of Commerce of New York, February 26, 1945.

Q. I doubt if it is good taste to be reading that stuff into this record; but if the Chairman wishes to allow it there, and if you feel it is good taste to read it into the record, do so. A. I had not any intention of reading it, but you asked if it was not too theoretical to be possible, and I replied that to my knowledge there was an instance of that precise thing being done.

Q. And you say your knowledge is based upon the fact that you read it in a publication? A. Quite.

Q. I think that is a good place to stop, as far as that goes, though you can give the name of the journal, if you like.

MR. MANN: I think he did. It is the Journal of Commerce.

THE CHAIRMAN: After all, Mr. Parker, the newspapers do hit it right sometimes.

MR. PARKER: Yes, of course they do; sometimes more often than we give them credit for, I think.

Q. That is the only case in which you ever heard of that being attempted? A. And I did not even hear of it until I had theoretically thought it out. It merely confirmed my theory.

Q. And you went looking for some confirmation of it? A. No. Somebody from the United States sent it up, after the brief had been filed.

Q. I do not suppose you would care to disclose who was good enough to help you to that extent. I do not want to know; you can tell me that privately. But really it is a bit far-fetched, is it not? A. I do not think I would say so.

Q. When we are trying to get something that is administratively possible and practical in the affairs of men as we know them in this country to-day? A. No, I do not think it is too theoretical; I think there is a danger there.

Q. Very good. Now I want you to look at pages 5 and 6 of your brief and compare them. There are two statements on those pages which have been bothering me, and I wish you would clarify them. On page 5 you have pointed out the similarity of operation between the stock company and the mutual. Then you go on -- I am coming back to this in a moment -- and I want you to direct your attention to the next clause:

"Both classes of investors are then entitled to a fair return on their capital from the profits of the business capable of being undertaken only after the required capital to do business has been provided, but only after income and excess profits taxes have been paid on such profits."

Then you underline the next sentence:

"No distinction can be made between assessments on capital stock not fully paid up and assessments on mutual subscriptions not fully paid up; nor between a partly paid stock certificate and an assessable note or subscription."

That is the matter of the premium note plan? A. Yes.

Q. You make them alike, unpaid subscriptions on share capital, and capital assessment on premium notes; you say to all intents and purposes they are the same, **that** they represent subscriptions to capital. That is your argument?

A. That is quite right.

Q. Now if you go back to page 6, where you talk about the income of mutuals, you say this:

"A mutual insurer must have a surplus of receipts over expenditures each year, unless it has a deficit. This surplus is income:

"(a) Interest from investments of the reserve or surplus funds is income of the corporation; (this is freely admitted under all systems of law and jurisprudence);

"(b) The surplus of premiums and assessment receipts over losses and expenses is also income and is 'annual profit or gain from any other source.'"

I thought on the other page you called that capital. Did I misunderstand you, or what did you say? A. Perhaps it might have been more clearly stated.

Q. I suggest it cannot be capital for one purpose and income for another. Which is it? A. It is collected as income.

Q. What? A. It is collected as income.

Q. Collected by -- ? A. By the corporation, as income.

Q. What is? A. The premium or the premium note, or the assessment on a premium note. The premium income, in whatever way it arises, is collected as income. Only subsequently is the difference perhaps appropriated as capital; but if it had been collected as capital it would have been repayable to the person from whom it was collected, so it was not appropriated as capital in the beginning. It was collected as premium, and is income. Subsequently an appropriation of a portion of that premium may be made as capital, into the assets of the company.

Q. Yes, but assessments on the premium note would only be made if they were required for reserves, would they not?

A. They would be required because the company needed the money. An assessment on the unpaid balance of a stock certificate would be in the same way.

Q. If they called it for that reason and used it for expenses and for the paying of losses, how does it become capital? Is it not either one or the other; or is it first one and then the other? A. I suggest that the latter is the correct understanding; it is first one and then may become the other.

Q. I was a little puzzled over that, but if that is your explanation -- ? A. Perhaps I should have done a better job on that.

MR. ELLIOTT: The same point, I think, is dealt with on page 9. I wonder if Mr. Ham would relate the sentence on page 9 to what he has just said.

"In other words, what an assured of a mutual pays in cash or as an assessment on a note as the consideration for the policy, is something distinct and different from his subscription to the capital of the mutual."

There the assessment is of two kinds, one what he gives as consideration for the policy, and the other his subscription for the capital of the mutual. I think this relates to the same point.

THE WITNESS: It does. My point on that is this. If it is collected as premium, or in premium income, that is what it is. If it is collected and appropriated as capital, then it is capital; but the premium income of a mutual company is invariably collected in the nature of premiums going into the coffers of the mutual, for the payment of losses and expenses. Subsequently, as operating surplus or operating capital, it is appropriated to the purposes of the corporation. But if it were in the first instance appropriated as capital, it would be returnable either to the person who put it up or his assigns. But it is not returnable at all when appropriated as premium, in any ratio to which he put it in.

BY MR. ELLIOTT:

Q. Is the contribution of a shareholder to a joint stock company a capital contribution? A. Yes.

Q. And is it returnable to the contributor? A. On the winding up of the company, yes. He owns his interest in it, which he can sell to his assigns, who may collect.

BY MR. PARKER:

Q. Does the amount paid on capital stock ever become

income of the company? A. No, I would not think so.

BY MR. ARNASON:

Q. When you were speaking of subsequent appropriations to capital after the moneys had been received as premiums, were you thinking of reserves, by any chance, or were your remarks to be confined to such a contribution? A. It depends on the sense in which the word "capital" is used. If it goes to the assets of the corporation it is appropriated as a capital asset of the corporation.

Q. You would exclude therefrom, then, refunds of gross premiums, would you, and consider as capital what was left in the company? Is that what you are driving at? A. My theory is that the dividends that you mention, the policy dividends are a distribution of surplus, or a profit.

BY MR. ELLIOTT:

Q. It seems to me that administratively it may be rather difficult to distinguish those assessments or contributions which are made as capital from those which are made as consideration for the policy? A. That is quite possible, Mr. Elliott. I do not think there is any difficulty in the joint stock structure; I think that is fairly clear. The trouble arises in the mutual structure, and at the moment I have not any answer from an administrative standpoint as to how it might be distinguished as between what was appropriated as capital and what came in as income. Generally speaking the bulk of what comes in, comes in as income. It might be that the assessment on a note to meet shortage of available assets -- I have not given any thought to that at all.

BY MR. PARKER:

Q. Just go back to page 4 of your brief for a moment, in the second last paragraph:

"It should be noted that the term 'carrying on business' as used in the Excess Profits Tax Act, 1940, has a very much broader meaning than the word 'trading' commonly used in England."

Why do you say that? A. I suppose I am speaking now as a lawyer.

Q. That is a statement of fact. To begin with, is the expression, "carrying on business" defined in the Excess Profits Tax Act? A. I am not certain; I would have to check that. I do not recall. The term is used; and that is the term that is used.

Q. I think that is correct. I do not care whether you are speaking of a lawyer or not. You state there is a difference and put everybody on guard, that they must not use those words interchangeably. What is the difference? A. I think I can carry on business and not trade.

Q. What does that mean within the provisions of the Excess Profits Tax Act; and what does "trading" mean as commonly used in England? You tell us there is a difference here, and in effect warn the readers of your brief to be on guard against that. What is the difference? Can you tell us, or do you suggest that we should look that up ourselves?

A. Without reference to the statutes I would not commit myself. I merely suggest that I might carry on business and not be trading.

Q. On what authority do you make that statement?

A. That is a matter of my opinion, which was asked for. I think the balance of that paragraph conveys the meaning.

Q. As long as I understand what you intend to warn us about? A. I think that explains the thought behind it.

Q. Now I refer you to the bottom of page 5:

"All insurance contracts are in essence and substance 'mutual' in the wider sense of the term."

We come back to this difficulty about the word "mutual" again. You say they are "in essence and substance mutual in the wider sense of the term." Is there any meat in that paragraph at all, or is it just filling? A. There may or may not be meat in it, but it seems to be the one principle on which all the briefs agree, that all insurance is, in its nature, mutual.

Q. I suppose all social activities can be said to be mutual in that sense; all government activities are mutual. Does it mean anything more than that? A. Yes, I think it does, in the sense of sharing the loss of the few, to use a cliché, amongst the many.

Q. Very good. Now I refer you to page 6, at the top of the page, where you say:

"The capital and reserves of both types of companies --" That is the mutual and stock, I take it? A. Yes.

Q. You go on to say:

"-- are the property of the corporation, in the assets of which, in the one case, the individual shareholders of the moment and, in the other case, the individual policy holders of the moment, have 'a right in respect of but not a right to.'"

What is that quotation from? A. I would not recall where the quotation comes from. I can delete the quotation marks and adopt the phrase as my own.

Q. It may lead us to some pretty good authority, that is all? A. I have not the faintest recollection.

Q. You cannot remember whether it is an apt phrase that came to you, or one that you read and took out of an insurance journal, or out of a decided case? A. I may have been the

author of it, and may have been afraid people would think I was, and put it in quotation marks.

Q. But quite apart from the quotation, whether your authority carries any weight or not, do you think the statement is true? A. Yes, I think the statement is true.

Q. Do you think that the reserves of the American reciprocals that were discussed here yesterday can, by any possible stretch of argument or imagination, be said to be in the same position as the reserves of a joint stock company? Can you not see any difference between them, yourself?

A. With respect to the reciprocals, yes.

Q. In respect to the ownership of those reserves?

A. Yes, with respect to the reciprocals.

Q. Then we will take them one at a time. You modify that statement in so far as your reference to the reciprocals is concerned? A. The heading mentions mutuals, and it had reference to mutuals as a group by themselves.

Q. You say now, speaking as you purport to do, I take it, and expressing the views of these joint stock companies --

A. Yes.

Q. You say that you do not wish that statement to apply to the reciprocals? A. No, because I do not think it does apply.

Q. You think that the reserves of the reciprocals belong to whom? A. According to the evidence --

Q. They are the property of whom? A. Of the subscriber, according to the evidence that is before this Commission.

Q. I do not care about the evidence. According to the evidence, plus your knowledge of reciprocals as an insurance man, to whom do the reserves of the reciprocals belong at any given time? A. They belong to the subscriber, subject to

penalties for taking them out.

Q. Do you agree that in connection with the reciprocals who were described here yesterday, where there is no organization, no association, no unit that owns anything, there is nobody there to tax at all, and that in this case the question of taxation is out, as far as they are concerned. Is that your position? A. There certainly is no corporate entity in the sense that there is in the mutuals.

Q. Is there anything to tax, other than the individual subscribers? A. The earnings.

Q. Is there any taxpayer? Is there anyone to tax other than the individual subscribers in the American reciprocals? A. There is a place it could be taxed.

Q. Where? A. In the hands of the attorney-in-fact.

Q. But who is to be the taxpayer, as distinguished from the bearer of the burden of the tax? A. Ultimately the bearer of the burden is the subscriber.

Q. I asked you carefully to distinguish between them. Who is to pay the tax; to whom is the tax collector to go and say, "You have something in your pocket, and I want it"? A. I cannot prophesy. If you ask for the possibilities, it could be taxed in the hands of the subscriber or in the hands of the attorney-in-fact.

Q. I am not asking you to prophesy. I am asking you if there is a unit, for want of a better term, or a group which can be called in law a taxpayer, as distinguished from an individual subscriber? A. I agree with the statement that there is not.

Q. You say there is not? A. No.

Q. Therefore does it not follow that in your view the Income War Tax Act, as presently in force, and the Excess Profits Tax Act just have no application to reciprocals? A. I do not agree with that.

MR. MANN: As at present enforced, do you say?

THE WITNESS: As enforced I agree with it.

BY MR. PARKER:

Q. I said in force, not enforced. In other words, there is nothing to come within the scope of the Income War Tax Act because there is nothing but the individual, apart from the individual -- there is no unit to tax?

A. I agree with that, that there is no unit to tax.

Q. What do you say as to the factory mutuals? Are they different? A. Yes.

Q. What is the difference? Why do they come in and the reciprocals stay out? A. Because the factory mutual is a corporation carrying on business.

Q. Is that all? A. Yes, I think that is sufficient.

Q. What about the next group, the mutual alliance? A. The same applies to them.

Q. And the same to the individual cash mutuals? A. The same to the individual cash mutuals.

Q. In other words, according to your view, the reciprocals are out, and the others are in; is that correct? A. No, I say there is no unit to tax.

Q. If there is no unit to tax, what else is there to tax, other than the individual subscribers? We are to the point where all the mutuals are expected to pay no tax on the business carried on by the so-called reciprocals, other than the individual subscriber? A. I quite agree as to the individual subscriber; but I think

the Income War Tax Act should apply to them as subscribers, or in the case of the attorney. I will not agree that they are different.

BY THE CHAIRMAN:

Q. Is it this, that the reciprocal is more nearly approaching the definition of mutuality than any other group? A. Yes, quite right.

BY MR. PARKER:

Q. I think you said that they not only are more nearly approaching it, but they approach it so nearly that they escape taxation as such? A. No.

MR. MANN: I am just wondering if my learned friend is asking about this matter as the law stands today, if he is referring to the law as it stands today, or as it might be.

MR. PARKER: No, I made that very clear in my question, when I said "as in force".

MR. MANN: I thought that you re-phrased your question.

MR. PARKER: No.

MR. MANN: If you are talking about the law as it is today, that is today, that is one thing, and if you are talking about the law as it may be recommended, then that is another thing. I want to have the distinction made, that is all.

MR. PARKER: I think you just inadvertently made a mistake as to who was reversing himself.

MR. MANN: I take it back, that you reversed yourself. I know counsel never reverses himself if he can help it.

BY MR. PARKER:

Q. Be good enough, please, to tell me whether you

understand me, that I am talking about the law as in force at the present time. You understood that all right, did you not? A. Yes.

Q. I am not talking about the ideal law, at all.

A. In the beginning I thought you were asking that.

Q. Then, we are getting to common ground on that.

A. Yes.

Q. Now, can we have this made clear: you think that the law as it stands today, and as it stood formerly -- that there is something or somebody in connection with those reciprocals today against which a tax should have been imposed, by reason of the nature of the situation? You say there was something there to tax? Do I understand that that is your statement? A. No, I say there is someone to be taxed, and that is the subscriber. He should not be allowed to deduct as expense his subscription and receive interest on it, clear of tax. Whereas, if he did not say, "I am a subscriber", but merely sets up a fund for himself, he pays the tax before he takes the money out of the surplus fund, and pays tax on income derived from the earnings of that fund he has created. But merely because he says he is a subscriber he gets a deduction as an expense of paying money to himself. That is so, if that theory is correct.

Q. Then, there is one question I should like to ask: we heard a great deal, a very considerable amount in fact in the brief, about the premium tax. It is suggested that there was discrimination under the Special War Revenue Act on the amount of premium tax paid with respect to joint stock companies, and the others.

A. I have heard a considerable amount of discussion

about that.

Q. Yes, but it is not right that there is any discrimination, I take it; or, is there discrimination? What do you say? A. There appeared to be apparent discrimination.

Q. Well, you say that there appeared to be apparent discrimination. I am asking you if, in your view, there is discrimination? A. Mr. Mann is producing another witness on the question, and perhaps it would be easier for the Commission to follow the theory through, after listening to him, than if I attempted to answer it.

Q. Well, you may have a very different theory from the next witness, and I should like to hear what you have to say. You are an experienced man, and you are the man who prepared this brief. I should think that you are the man who would deal with the questions discussed in the brief. A. I drew the brief, along with counsel.

Q. You say you take the responsibility for it. I should like to have your idea on that question. I should not like to pass it on to some other witness, because he might say that you did it, and that you are the one to answer it. Just straighten us out on that point, because we want to know the whole story. A. Well, what is the question?

Q. I shall take it step by step. Joint stock companies do pay net premium taxes, is that correct?

A. Yes, net premium taxes.

Q. They pay net premium taxes? A. Yes.

Q. Not gross? A. No.

Q. They pay 2 per cent on something? A. Yes.

Q. And it is on what? A. It is 2 per cent on the net premium income.

Q. What is the net premium income in a joint stock company? A. Gross, less refunds and cancellations.

Q. Is that all; get it down so that we will have something upon which we can rely. Let us first consider gross premiums. Let us say that I come to you and pay you a premium to insure my house for \$100. That, of course, is a gross premium. A. Yes.

Q. Out of that on what do you pay the 2 per cent? You do not pay it on the full \$100, do you? A. Yes, unless you intended us to re-insure it. Licensed re-insurance is off.

Q. And if I stay there for my full time, whether it is one or three years, you pay 2 per cent on that \$100 on the year in which I pay you the \$100? A. Yes.

Q. With nothing deducted whatsoever? A. Nothing deducted whatsoever.

Q. You are talking about this particular \$100? A. Everybody's \$100.

Q. That is paid in during that year? A. Yes, that is right.

Q. Is that right? Is that what you paid the premium tax on? A. So far as I know, yes. I am not the company; I do not pay the tax. That is the difficulty I foresee for myself in answering that. I am not the company.

Q. If you are not competent to straighten it out, I shall not stress the point. A. I admit my incompetence on the point.

Q. All right. Then, one other thing on which I think you can help us. Perhaps I am getting in over my head here, too.

MR. MANN: You have not got in far over your head,

yet.

BY MR. PARKER:

Q. We have heard a good deal about the tax burden, and about taxpayers and so on, and have heard about direct taxes and indirect taxes. In the ordinary joint stock company, do you in your manner of thinking, or, perhaps I should say in your approach to the whole subject, make any distinction between the taxpayer and the person who bears the burden of the tax? A. I do not believe I follow you.

Q. Well, take the ordinary joint stock company. It makes profit, and I know that the company is a legal entity -- I think we have heard that expression before -- or is a person, a legalistic person, or something like that; it is a person, under the language of the Income War Tax Act, and the Excess Profits Tax Act of 1940, as well as a taxpayer? A. Yes.

Q. And the tax is imposed upon that person, an artificial person, if you like, but a person nevertheless, within the meaning of the law? A. Yes.

Q. But by reason of the fact that it is an artificial person, or a legal person as distinct from a human being, can it be properly said that the corporation bears a burden of the tax at all? Would it not be more correct to say that the burden of the tax is borne by those who would have received money if the artificial person had not had to pass that on to the government? A. Is that not rather a question of the use of words? I do not think your question can be answered yes or no. In the first instance the corporation bears it, and ultimately the person whose income is reduced by the amount of it bears it.

Q. You make a distinction between bearing the burden of the tax and paying the tax. I suggest there ought to be a difference and that we ought to approach it from that angle, if we are looking for a fair, just and equitable system of taxation. A. You see, the difficulty is this; supposing the corporation is paying no dividends at all. The shareholders of the moment, and the amount of the tax makes no difference as to whether a dividend was paid. The shareholders would not have borne anything. It is paid by the shareholders before the dividends are paid, and reduced by the amount of the tax.

Q. If nobody pays a tax there is no burden to bear, that is true. But may it not be that someone pays a tax, and someone else bears the burden? A. I quite agree that that is possible, and often true.

Q. So that, searching for an equitable basis of taxation, you agree with me that we should keep our minds focused on the person who bears the burden rather than on the person who might be likened to a mere amanuensis. Should that not be kept in mind? A. There is no harm in keeping it in mind. I do not know whether it is a sound theory to work upon.

Q. You do not agree that that is the proper way on which to approach it. A. I have my reservations on that theory.

Q. Well, that is all I have to ask you.

BY MR. VAUGHAN:

Q. May we explore recommendation (b) which says, at page eleven:

"That the tax on income and profits in respect of unincorporated bodies such as reciprocal exchanges and inter-insurers who act through an attorney-in-

fact, be assessed to income tax upon the respective members."

What would be the procedure in doing that? A. It might be a difficult job, I agree, actually to draft a section which would accomplish it, and accomplish it fairly. I am not competent at the moment to give you a formula for it.

Q. Those individual members, assuming that they are corporations, do they not pay already -- that is, on their rebates? Rebates increase profits, and they pay more on their profits. A. But if you accept the theory that they are self insurers, or just insuring each other, they have already taken a deduction in the expense item by the amount of the money they have put up.

Q. That is, the expense reduces their profits to that point? A. Yes.

Q. By merely moving from here to there they have increased the expense and reduced the tax item. While they leave it there it earns money, which money, when it flows back, may lower that expense item. A. But they cannot create expenses by paying it to themselves.

Q. I am wondering if they have any plan of carrying that into operation. You have no different plan by which it can be done, have you? A. One might be evolved, but I certainly have not given it any thought.

Q. Then, take the second part, which states:

"And that the attorney-in-fact be assessed to income tax and excess profits tax in respect of the income and business profits of such organization remaining in his hands."

As an agent, or an attorney-in-fact, in that capacity he would be paying income tax, would he not? A. Yes, in

his capacity as carrying on business. But this is just funds held by him on behalf of others.

Q. Let us see that again. It states:

"And that the attorney-in-fact be assessed to income tax and excess profits tax" -

and so on. It looks as though it would be personal assessment against him. A. It was not intended as such. He would be assessed as a citizen, and for the business he carried on. But this is money of the subscribers while it remains in his hands.

Q. I understand that. First the subscribers would be assessed, according to some formula, and then this is just a second tax that the attorney would be assessed; is that correct? A. No; with respect to what they get they would pay, and what he holds on their behalf he should pay.

Q. The attorney? A. Yes, he distributes the money. If there is a tax on that the subscriber should pay it. Then, if there is income that he retains it should be taxable in his hands on behalf of the subscriber who would have paid the tax on it if he had got it.

Q. Well, do not those two overlap? First of all, the subscriber is taxed, and then the attorney is taxed on behalf of the subscriber; there would have to be some distinction. A. If there was a dollar of income and he distributed 50 cents of it, to the subscriber, that should be taxed; and the 50 cents of income that he still holds as an agent for the subscriber should be taxed. That is the purpose of the paragraph, although probably it is not very clear.

Q. It is difficult to see how it could be operated,

that is all. There was some discussion yesterday about British fire insurance companies being exempted from taxation here. A. Yes.

Q. You represent some of those, I understand?

A. Yes.

Q. Also you represent Canadian fire insurance companies which do business in England? A. Yes.

Q. Are those Canadian companies taxed in England, do you know? A. My impression on that question is that the income of those companies is all subject--investment income--is all subject to tax in some jurisdiction, and that that likely is the jurisdiction of domicile.

Undoubtedly the Canadian government has taken care to protect the interests of its Canadian corporations operating in foreign fields by reciprocal arrangements with respect to what happens to investment income of Canadian companies operating in the United States, and United States companies operating in Canada. There are reciprocal tax arrangements.

Q. You think there is some reciprocal arrangement?

A. Yes, and all that income is subject to tax in some jurisdiction. I presume one difficulty they would find in the insurance business would be a Canadian jurisdiction taxing what is said to be profits by investment of British companies in Canada, and so on. Those investments are not in Canada at all. They are held by the fiscal agents in New York or London. The physical reserve might not be in Canada at all. It might be earned in foreign countries, and not Canadian earned at all.

Q. As we understand it, insurance companies tax all premiums. A. The Canadian companies pay to the Canadian government on total income, - investment,

premiums and anything else - any income they have. They pay on total income.

Q. Is there any chance that British companies are being exempted here and Canadian companies are being taxed in England? Do you think there is any possibility of that? A. No, I would not be able to express an opinion, but I think there would be reciprocal tax arrangements between the British and Canadian governments, because there are Canadian companies operating in England. I am quite satisfied Canadian companies would not permit themselves to be placed at a disadvantage by way of taxation.

Q. We can have that looked into. A. Yes.

BY MR. ELLIOTT:

Q. Do you know whether foreign companies in making their Canadian income tax returns are permitted to deduct, as expenses, treaty re-insurance expenses? When they have treaty re-insurance expenses, with some other insuring concern, and make payments for it outside of Canada, is the payment they have to make permitted as a deduction? A. Mr. Hurry may know that; I do not know.

BY MR. VAUGHAN:

Q. One more question: in the beginning of your examination the question as to the terms mutual, reciprocal and cooperative came up. You mentioned about those terms being interchangeable. Do you mean they are interchangeable regarding cooperatives and mutual fires, or do you go so far as to say it is interchangeable in those different types of organizations? The reason I ask the question is this, that Mr. Hayden was speaking the other day and pointed out the difference between cooperatives and mutual fire. He said that in a

producer cooperative there was business with the public, that is, the producer provided his product to the cooperative, and the cooperative sold to the public, but that in fire insurance they dealt entirely with themselves. I am wondering if you disagree with that.

A. It is really a matter of definition, and use of the term. It happens that during the last seventy-five years cooperatives have been operated in connection with merchandising needs of consumers and producers, and the word "mutual" is one which has been used more or less in connection with insurance. But the term "mutual" is used as one of the reasons for a cooperative. Then, the term "reciprocal" has also been applied to insurance. But the Saskatchewan legislature provides for cooperative insurance companies, and I presume we are just playing with words.

Q. Do you think there is a difference between a merchandising cooperative and a mutual fire insurance company?

A. I think there are many differences. They operate on the same principle, but the one fact that one deals in a promise to pay in the future, and the other deals with something in hand necessarily creates a difference.

Q. So far as the commodities they deal with are concerned; but do you think there is any difference with respect to taxation?

A. That is, that a mutual corporation might or might not be taxed, and that a cooperative might or might not be taxed, do you mean?

Q. Senator Hayden pointed out that here was a mutual fire company, the members of which dealt among themselves. Here is a cooperative, and they finally deal with the public.

A. There again the Mutual Fire Insurance Com-

pany, if they say that every policy holder is a member, that would very well deal with any question of direct insurance with anybody but themselves. But I submit that when they accept re-insurance from other mutual corporations, or cede re-insurance to them, that they are then dealing in the insurance business with someone other than their own members. Because re-insurance business is almost as big as direct business. There is a very big business in re-insurance, in dividing up and spreading risks.

MR. HAYDEN: Not with the Mutual Alliance group.

BY MR. ARNASON:

Q. In connection with that: if it were possible to differentiate between strictly mutual business done by a company, as compared with non-member business, referring here to some of the submissions which have been made with respect to cooperatives, in so far as a cooperative does business with non-members, to that extent it may be said to make a profit; do you think there is any reason why a mutual insurance company should not be exempt on its strictly mutual end of the business? Is there any reason why such a mutual insurance company should not be exempt on business done on another basis? Perhaps I have not put my question very clearly. A. I follow you.

Q. All right, could you answer that? A. My answer is no, because those in the mutual end of the business are a group of people pursuing a business venture with the public generally, and on that account should be subject to taxation, the same as a group of shareholders who are a group of people pursuing a commercial venture.

Q. Do you mean that there should be taxation on all

business, or just that portion of it done with the public?

A. I would say on all their business.

BY THE CHAIRMAN:

Q. Mutuality is a more comprehensive term, which embraces cooperatives and reciprocals, or whatever you have. A. Yes.

Q. And mutuality is the basis of the whole theory. A. Yes; and I would suggest this, depending of course on the tax level, that if you allow one group of people tax free on their mutual business, you certainly help them in their pursuit in the competitive field of their other business.

BY MR. HAYDEN:

Q. I should like to ask one or two questions. In discussing this matter of investment income of joint stock companies, British and foreign joint stock companies, is it right to say that you represent a number of them? A. Yes.

Q. And you can tell us whether or not the investment income of those companies is or is not calculated in your Canadian income tax return for tax purposes. A. I cannot tell you definitely. I can say I do not think it is, but I think Mr. Hurry can answer that question better than I can.

Q. So far as the Mutual Alliance group is concerned, they are in the category of foreign mutual companies, are they not? A. Yes.

Q. And if the tax scheme was enlarged to provide for an assessment of income tax on the Canadian investment income of foreign mutuals, then as between them and the investment income of your British and foreign joint stock companies there would be discrimination, would there not?

A. Yes, undoubtedly. I do not think anybody is urging that.

Q. I understood from your brief that you were singling out, as the badge for taxation of mutuals, the fact that they have investment income. A. No, if exemption is granted because of their status as foreign or British companies, stock companies, I would say that the same exemption should apply to mutuals. But I was talking about mutuals, and in the brief we were talking about mutuals, as such, and not their domicile.

Q. You agree there is no tax discrimination at the present time in our Canadian tax structure and in the administration of the statute, so far as investment income is concerned as between British and foreign joint stock companies and foreign mutual insurance companies operating in Canada? A. Certainly if neither are taxed, there is no difference.

Q. All right. With respect to premium tax, your companies pay 2 per cent? A. Yes.

Q. And on the basis of net premium; and the Mutual Alliance group which I represent are being assessed on a basis of gross income, including dividends paid to the policy holder on a 3 per cent basis. So that you would not suggest that there was any tax discrimination at the present time working against your competitive insurance business in Canada, so far as the Mutual Alliance group is concerned? A. There seems to be two points there, and one of them I shall try to answer. On the question of net or gross premium, may I say that those terms have a special meaning in the business. On the basis of net premium, being refunds and returns for cancellations, and re-insurance with licensed re-insurers, on that

basis I submit that the members of the American Mutual Alliance, apart from the one to two or two to three factor, pay on the same basis exactly. If I understand the complaint it is that the dividend ---

Q. Oh, I am not complaining; I am just asking you a question. My question is not a complaint in any way, to you; if I have any complaint to make it will go somewhere else. I am asking whether under those circumstances you are suggesting there is any tax discrimination working against your joint stock companies.

A. There would be a discrimination against joint stock companies if the members of the American Mutual Alliance paid on their net premiums less their dividends instead of on their net premiums including dividends. I would say there would be a discrimination against joint stock companies in that case.

Q. On what do you say joint stock companies pay?

A. On their net premium.

Q. And then you suggest that if mutual companies paid on their net premiums, that that would constitute a discrimination against joint stock companies.

A. I do not agree that the net premium less dividend is a net premium.

Q. You assert that the dividend returned to the policy holder should be included in the description of net premium, is that correct? . A. Yes, that is correct.

Q. Until 1942 your joint stock companies enjoyed the privilege of deducting the premium tax paid under the Special War Revenue Act, from your income tax -- directly from the income tax? . A. I believe that is correct.

Q. Payable under the Income War Tax Act? A. That is correct.

Q. So that that was a direct deduction of tax from tax, so that you had reflected into income tax payments a credit for the amount of the tax you paid under the Special War Revenue Act. A. We paid the Special War Revenue Act, and paid that much less under our income tax.

Q. Yes. Since 1942 you have, by virtue of an amendment to the Income War Tax Act -- you have been permitted to deduct your premium tax payable under the Special War Revenue Act as an item of expense, before calculating your taxable income subject to income tax; is that correct?

A. There again, I am not a taxpayer, and I am not certain. I am not certain about that.

Q. You must be a taxpayer, surely? A. In my personal capacity, yes, but not as an insurance company.

Q. You are not a taxpayer in respect of this item? A. No. I think possibly Mr. Hurry can give that information, but I cannot answer it.

Q. You were aware there were some changes in the income tax of 1942 affecting the taxation of joint stock companies? A. Yes, I remember reading that, that is all.

Q. To that extent, and by reason of the fact that the mutual operations were not subject to any of those taxes, competitively there was no advantage or disadvantage, was there, to one company or the other?

A. Not being clear as to the effect of the taxes, I cannot answer that.

Q. Look at your brief. I am curious to learn the meaning of the statement you made at page eight of your

main brief. I do not like to give it a title, so I shall simply call it the main brief. If I were to put a name on it you might misunderstand me. Under the heading "Exemptions amount to a Government Subsidy" you say:

"Mutuals being free from taxation on their surpluses and investments can afford to allocate to their members and other assureds the amount of which the state has been deprived by reason of the exemptions."

A. Yes.

Q. And then you say:

"The effect is clearly a state subsidy in favour of mutual policy holders or members, and is class discrimination to the disadvantage of all other Canadian taxpayers."

Do you not think that, in the light of what we have been discussing, that statement should be qualified?

A. I still think it stands.

Q. You still say that it is not a subsidy when the British and foreign joint stock companies are not subject to income tax on their investment income? And you still say it is a subsidy when the Mutual Insurance group is not subject to income tax on its investment income?

Do you say that? A. Yes, that is exactly what I say, because my understanding is that this question with respect to the British and foreign companies is a reciprocal arrangement by the Canadian and foreign governments, each in the interests of their own corporations and creatures.

Q. But I do not think you have answered my question. If you think you have, I shall stop at that point. But you have said that the fact that the mutual

companies operating in Canada do not pay income tax on investment income is the equivalent of a state subsidy. I have pointed out that so far as British joint stock company operations in Canada are concerned, they enjoy the same privilege. A. I did not get the significance of your question. You are suggesting that a foreign mutual being free from taxation ---

Q. Yes. A. You suggest if foreign corporations are exempt under any reciprocal arrangement, it should apply to any foreign mutual corporation the same as a foreign joint stock company.

Q. But to the extent it has been developed here, in respect of your statement as to the exemption of the foreign mutual company from income tax in Canada on investment income, you say that is a state subsidy, or that it is tantamount to a state subsidy. I suggest it is equally tantamount to a state subsidy when you exempt British and foreign joint stock companies on their investment income in Canada. A. With respect to foreign mutuals being free from taxation on their investment income, that certainly does not amount to a state subsidy any more than a foreign joint stock company to be free.

Q. If it does not amount to a state subsidy there is some mistaken application in saying that it is tantamount to a state subsidy. A. That does not say foreign mutuals.

Q. Then, am I to read this paragraph as being restrictive in relating only to Canadian mutual corporation operations? It is not intended to be general in its application. A. The statement applies to mutuals generally, subject to any other exemptions that

may exist for some other reason. There may be entirely different reasons for which they may be exempt.

Q. Notwithstanding what we have been saying, you are not prepared to amend this statement? A. No, I am not prepared to amend it.

Q. Then, I was interested in your answer to a question asked by one of the commissioners with respect to farm mutuals. I gathered that you agreed that if you had a farm mutual serving a local farming community, and even having some income from moneys on deposit in the bank, I think you said that strictly the income might be subject to tax, but you agreed that there might be other considerations which would put it in the category of a mutual, in which it should not be subject to tax; is that correct? A. Yes.

Q. And you agreed that it did not matter as to the size of the farm mutual? I think you said the size did not matter. I think that was the answer you made to the question. A. I said size was not an element to determine; it was the field it which they operate.

Q. Nor the fact that it might be incorporated would not be an element, either, would it? A. I think you are stretching my answer to Mr. Arnason farther than it need be stretched. I merely meant to imply this, that if it should happen to be government policy, the policy of the government of the day, to add another benefit to farmers with respect to exclusive farm mutuals, I do not think that so far as my principals are concerned, they would be concerned enough with it to raise any issue in the matter.

Q. But what I am trying to get at is this, that I want to see whether the intervention of this situation

of a corporate entity should change your consideration of the problem in trying to arrive at a principle as to whether the tax should or should not be paid. A. The corporate entity is a very important factor in it.

Q. If a farm mutual were incorporated, and was acting in the manner in which we have discussed it, you would say it should be subject to tax? A. It should be subject to tax, subject to what government policy may be with respect to farmers.

Q. You do agree, then, that when principles are being considered, when you are deciding whether or not income tax should apply to mutual operations--so-called mutual operations, and that there are principles greater and broader than the mere fact that you may have interposed a corporate structure. A. Do you mean from the standpoint of government policy or from that of logical argument?

Q. From the standpoint of any approach to the problem of the taxation of mutuals. A. No; from the logical standpoint I think the interjection of a corporate entity is one of prime importance.

Q. Why? A. Because it is an entity.

Q. Do you say that because an entity exists that it should be taxed? A. The government seems to think it should be taxed in most cases of entity.

Q. I beg your pardon? A. The government seems to think any kind of an entity should be taxed, these days, and I suggest that that being an entity it is properly subject to tax.

Q. Do you not agree that the ultimate burden of taxation is a factor, in considering whether or not you should tax any corporation in any field? A. Will you

put that question again? This is getting rather into the realm of economics, I think.

Q. We are not confined to the realm of law in this matter. A. I am trying to follow your question.

Q. I am asking this: do you agree that in attempting to establish a policy for taxation that the ultimate burden of such taxation--that is, where that taxation will ultimately fall and ultimately be paid--is or is not a factor?

THE CHAIRMAN: Do you think that is covered by our terms of reference?

MR. HAYDEN: Yes, but I shall limit it to the mutual insurance field. If I appeared to be too general, let me say that all my questions are directed to the field of mutual insurance.

THE WITNESS: May I try to interpret your question, then? You are asking this: do I think that because in the last analysis a tax imposed upon a mutual corporation would be borne by the policy holder -- should that fact not be given consideration. Is that what you are asking?

BY MR. HAYDEN:

Q. Yes. A. No, I do not think it should.

Q. Why not? A. I cannot answer that. I just do not think it is on sound ground.

MR. PARKER: The answer should be: why should it?

BY MR. HAYDEN:

Q. Are you aware that in the field of taxation the taxing authorities have been looking beyond the cloak of corporations, and have been taxing what lies behind those corporations?

MR. MANN: Surely that type of question should not be allowed -- as to what somebody else does somewhere

else at some other time.

THE CHAIRMAN: I think it is relevant to the issue.

MR. MANN: How can he answer it?

THE WITNESS: Sometimes it is a ground, quite.

BY MR. HAYDEN:

Q. You agree that sometimes it is a ground, but you say that with respect to the field of mutual insurance it should not be a ground? A. That is exactly correct.

Q. Well then, you agree, as a prudent insurance man, that the establishment of and the maintaining of reserves in excess of the statutory requirements is a prudent act?

A. Undoubtedly, yes.

Q. Then, do you not think, that it is a prudent act from the point of view of the policy holder? A. Yes, from the point of view of everybody.

Q. The point of view of the shareholder? A. Yes.

Q. I suppose it would make more certain the maintenance of his capital investment? A. It makes more certain the chances of a claim being paid, yes.

Q. Would you subscribe to the principle that to the extent that reserves are established in addition to the statutory reserves, and earmarked for the policy holder, that they should be tax free?

MR. MANN: Would you mind repeating that question?

THE WITNESS: I do not think that the mere fact that a thing is a good thing is a reason why it should not be taxed, necessarily.

BY MR. HAYDEN:

Q. I am asking whether you subscribe to what I have said. A. I do not think so.

Q. In other words, you think that in the operation of a joint stock insurance company, to the extent that

you might set aside reserves and earmark them for the policy holders' accounts, over and above statutory reserves, that those reserves should first be subject to income tax? A. I cannot see any reason why they should not. That is, I would say that if the country needs money.

Q. You appreciate that the effect of taxing those reserves is to increase the cost of insurance to the policy holders? A. Yes, of course.

Q. It does not increase or decrease the benefit to the shareholders, does it? A. What does not decrease the benefit to the shareholders?

Q. To the extent that you set aside reserves you increase the cost to the policy holder. A. To the extent that you tax reserves?

Q. Yes. A. What is the next question?

Q. And then I say that by that act you do not decrease the return to the shareholder? A. Certainly you do.

Q. Will you explain how that can be, because if you increase the cost to the policy holder you increase the payment of the policy holder to take care of it; is that not correct? A. Ultimately the consumer, I suppose, generally speaking, will pay all taxes. But the immediate effect of it, in the first instance, is I presume, upon the shareholder.

Q. Why? Do you mean that he has a smaller shareholder profit available for payment of dividends?

A. To the extent that the corporation pays taxes the amount available for dividend is reduced. The amount that the dividend is reduced, the capital value of the stock is so much less if he wishes to sell it.

Q. You do agree to certain things, that is, if you set up a policy holder reserve which has to go through the wringer of taxation, then the policy holder has to contribute more in order to maintain the same reserve.

A. Yes.

MR. MANN: I am impressed with the fact that this witness is not an underwriter. He is not an insurance manager, and has so informed the Commission. I think it is a little difficult, when he has qualified himself not as an underwriter, to ask questions which are so much directed to the process of underwriting. I have a very expert underwriter here, and I do not know why Mr. Ham is being questioned as to underwriting questions, when this other witness is available.

THE CHAIRMAN: He has the privilege of saying that he would prefer not to answer. He has told us on several occasions that he would prefer not to, and he can say it again if he wishes.

MR. MANN: I draw attention to the fact that the examination has practically reached a pinnacle of futility with respect to underwriting questions asked of a non-underwriter. That is all I wish to say.

MR. HAYDEN: There is no pinnacle of futility, so long as Mr. Ham continues to answer. He is free to say he does not care to answer, or has not sufficient experience, if he wishes. These are not underwriting questions.

MR. MANN: What are they, then.

MR. HAYDEN: And, so far, I can find support in the brief for every question I have asked.

THE WITNESS: I am prepared to try to answer them as long as I can.

MR. MANN: Answer them if you can, and if you cannot

answer them, just say so.

BY MR. HAYDEN:

Q. In order to establish a reserve, even a statutory reserve which you in your wisdom would say was advisable for the prudent insurance man to do, to the extent that that reserve which you would create out of your earnings would be subject to taxation, you would have to get more from the policy holders and from payments in to maintain the same reserve? A. Yes.

Q. The effect of that would be to increase the cost to the policy holder? A. Yes.

Q. How would it decrease the benefit of the shareholder? A. I understood you to be talking about mutuals a minute ago.

Q. No, I am talking about joint stock companies. A. Oh, I thought you were talking about mutuals. I will have to follow it back again, because I was thinking about mutuals.

Q. Well, I said, "joint stock companies". A. The answer to that, as I see it, is this, that taxes do not affect the insurance business the minute they are put on. The tax is imposed, as it is on joint stock companies, at the moment, to that part of the surplus allocated to reserve. Ultimately premiums have to take care of it, and ultimately premiums have to be raised to take care of it. In the meantime the weight is borne by the shareholder.

Q. Then, I suppose if the principle of maintaining these reserves is sound, it applies equally to mutual operations? A. Absolutely.

Q. And in a mutual operation, where the shareholder element is missing, then you agree also that to impose a

tax upon a hold-back, or reserve, since such hold-back or reserve is necessary, would increase the cost of the insurance to the policy holder. A. To the mutual policy holder, yes.

Q. And, in effect, would it not be this, that the mutual policy holder--and I am talking about the Mutual Alliance only--contributes a premium which he knows at the time he contributes it is on the mutual plan, and that while it is a maximum it is not the fixed and determined amount of the premium? A. I shall have to disagree with those points. I think it is a fixed premium.

Q. You think it is? A. Yes.

Q. You understand what is meant by mutual insurance, according to its statutory definition? A. In Ontario?

Q. Yes; and the other provinces. A. Yes.

Q. That is, it is not a pre-determined amount.

A. My own judgment is that it is a pre-determined amount.

Q. Do you apply that to the method in which the Mutual Alliance group operates, when you say that?

A. No.

Q. I am talking about the Mutual Alliance. A. It is a fixed premium.

Q. You say it is a fixed premium? A. Yes, because I do not conceive that the dividend is a return of premium. It is a division of surplus.

Q. We differ on the interpretation of the fact.

A. Yes.

Q. You have read the provisions in the policy, the specimen policy, of the Lumbermen's? A. I guess I have seen it, but I do not recall actually.

Q. Then, do I understand your proposition to be this, in connection with Mutual Alliance operations,

that if a policy holder pays \$100 on a mutual insurance plan for his insurance, and at the end of some period of that policy there is returned to him \$20, you say that that item of \$20 should be taxed as income of the corporation, rather than be regarded as a return of a portion of the premium which was not required or not needed for the purpose of operations of that mutual insurance company? A. I shall have to have your interpretation of what you mean by insurance on the mutual plan.

Q. I have told you that. I have referred you to the statutory definition of the various provinces, and you have said that you are familiar with them.

A. Yes, and I say that is not in my judgment insurance on the mutual plan, because it is for a fixed premium.

Q. That is where we differ. You would agree, then, that if Mutual Alliance operations were in accordance with the definition of mutual insurance as contained in the various provincial statutes, and that the premium was not an exact and pre-determined amount, but only a maximum amount -- then you would agree, would you, that the return of the so-called unabsorbed portion to the policy holder would be a reduction in cost and in income of the corporation? A. I certainly would not admit that.

Q. Whether you admit it or not, it does not matter whether the premium is a fixed amount or an indefinite amount -- only a maximum amount. A. I do not follow that question, at all.

Q. You have told me that you do not agree that what I have said applies to the Mutual Alliance operations, because in your opinion the premium that a Mutual Alliance policy holder pays is a fixed amount.

A. Yes.

Q. Then, suppose that the Mutual Alliance operation is in accordance with the definitions contained in the various provincial statutes, of a maximum amount, but not a pre-determined amount; in those circumstances would you agree that the return of the \$20 would be a return of the unabsorbed portion of the premium, and could not be regarded as income in the hands of the corporation? I believe you have said no to that also. So I say, then, that your judgment does not proceed on the basis of anything except that no matter how the mutual plan operates, a return to the policy holder of anything should be subject to taxation in the hands of the corporation.

A. You must have missed what I said. I will re-state my position. I do not think the method of operation of the Mutual Alliance group is on the mutual plan, being for a fixed premium.

Q. Because, in your opinion the premium paid is a fixed premium. A. Yes; my further opinion is that amount of revenue reported in respect of estimated costs over actual costs is a division of profit or surplus to the policy holder out of that venture. Now, where do we get after that? I do not follow your words as you set up the other proposition. If my statement now clears the air, so far as you are concerned, then that is my position.

Q. I have asked you if the operation is in accordance with the requirements of the definition of mutual insurance as contained in the various provincial statutes. A. I do not know the various definitions.

Q. You know the Ontario statute. A. Oh, I have looked at it in the preparation of this brief, and I know

it says something about being on the cash plan, and refers to the maximum amount, and so on; but I would have to have it in front of me to give a legal interpretation of it.

Q. I am not talking about a legal interpretation. If we get to that point I will not press the question.

A. I cannot answer it without the statute in front of me.

THE CHAIRMAN: Well, we will let you see the statute during the luncheon hour.

The Commission adjourned at 12.30 p.m.

AFTERNOON SESSION

Friday, April 20, 1945

The commission resumed at 2.15 p.m.

A.LESLIE HAM,

Examination continued

BY MR. MANN:

Q. There was an answer to a question left up in the air at the adjournment, Mr. Ham. A. That is correct, sir.

Q. Will you go on with it? I have forgotten the exact terms of the question, but I know it was left up in the air.

A. Mr. Hayden enquired about my understanding of business on the cash plan. Subsection 43 of the Ontario Insurance Act defines mutual insurance as follows: "Mutual insurance means a contract of insurance in which the consideration is not fixed or certain at the time the contract is made and is to be determined at the termination of the contract or at fixed periods during the term of the contract according to the experience of the insurer in respect of all similar contracts whether or not the maximum amount of such consideration is predetermined." Now, if we take the case of the members of the Mutual Alliance group and suggest that the consideration of the contract is not the premium, that is that it is not on the cash plan, you find it very difficult then to reconcile the situation that would exist under a fire insurance contract which has on it statutory condition No. 10 with respect to the termination of the insurance, because it reads: "The insurance may be terminated: (a) subject to the provisions of condition 9"-- condition 9 merely is protecting the rights of mortgagees and other payees, --"by the insurer giving to the insured at any time fifteen days' notice of cancellation by registered mail, or five days'

notice of cancellation personally delivered, and, if the insurance is on the cash plan, refunding the excess of premium actually paid by the insured beyond the pro rata premium for the expired time." Now, if a contract with a member of the Mutual Alliance group is not on a cash plan, then that statutory condition means that they do not have to return anything to the insured of the consideration which they had received. If their business is on the cash plan, then this provides a statutory right for the insured to get back pro rata -- subsection (b) says: "If on the cash plan, by the insured giving written notice of termination to the insurer, in which case the insurer shall upon surrender of this policy, refund the excess of premium actually paid by the insured beyond the customary short rate for the expired time." There again in the case of cancellation by the insured there would be no necessity of refunding anything. If he cancels the policy the first day he keeps all the premiums because it only applies to business on the cash plan. For that reason I suggest the consideration of the contract with respect to these companies is the premium, and that they are on the cash plan.

MR. MANN: Otherwise the statute means nothing.

BY MR. HAYDEN: That is the basis for your answer to me-- that the Mutual Alliance operates on a fixed premium?

A. Quite, yes.

Q. Because of this cancellation provision? Do you know how the mutuals deal with cancellations? A. I have no idea. I have never carried one of their policies.

Q. I think it is a fair question to ask you whether or not you know. You heard the evidence of Mr. Gruhn as to how the Mutual Alliance group operates? A. Yes.

Q. And that they do operate on the mutual insurance plan?

A. He so stated.

Q. You are not familiar with the manner in which they operate, are you? A. No.

Q. But now you are presenting as an argument the fact that the cancellation provision is such, you say, that they must be operating on the cash plan? A. That is my conclusion.

Q. Why? -- because they could not otherwise pass back to the policyholder all that he might be entitled to? A. No, I didn't say that, sir. I said there was no obligation on them to pass anything back. They can, certainly, but there is no obligation, statutory or otherwise.

Q. I suppose there is no obligation upon them to operate in the insurance field; but are we not concerned with the method which they do follow in operating? A. I suppose that is what the commission is concerned with.

Q. Then one question might summarize what we were discussing this morning -- and I have to put in a little preamble, if you can bear with it. If you take your British and foreign joint stock companies on the one hand; they have an underwriting gain or profit, and they have investment income; is that right? A. Assuming they have, yes.

Q. Let us assume they have; then for the purposes of considering income tax in relation to these companies we do not look at the investment income? A. I presume they do not, no.

Q. That they look at the underwriting gain. Now, take the foreign mutuals, the mutual alliance group. Have we to set them in the same perspective, for the same reason that we set aside investment income and look only at the underwriting gain; is that right? A. Right.

Q. Now then, this, I understand, is your proposition: that that underwriting gain when it accrues to the stock company is subject to income tax; is that correct?

A. That is correct.

Q. And you say that that underwriting gain at that point in the hands of the mutual insurance company should also be subject to income tax?

A. That is correct.

Q. Now, there is no mixture of funds there; it is just underwriting gain we are talking about -- is that right?

A. Yes.

Q. And you say that regardless of the fact that in the case of the mutual insurance operation that underwriting gain is returned in substantial amount to the policyholders?

A. Quite, yes.

Q. You do not regard the position as being at all different because in the case of the joint stock company it is the shareholder who is entitled to the proceeds of that fund?

A. No, I cannot say that.

Q. And your understanding as to who is entitled to that amount, that underwriting gain, is not regarded by you as a factor of any importance at all in considering whether or not income tax should apply to that fund?

A. In this particular case, no. It may be a factor with other sorts of corporations.

Q. We will come to your strict mutual in a moment. Then in the case of the foreign mutual, that underwriting gain going back to the policyholder reduces his cost of insurance, doesn't it?

A. Yes. In any event it reduces his cost.

Q. And in the other case of the joint stock company in going on to the shareholder it does not affect the cost of the policyholder?

A. No.

Q. Unless income tax has some effect on the insurance cost of the policy holder?

A. Yes, quite.

Q. So you cannot see in principle any difference in approach to the problem of taxation by that so-called underwriting gain in that form? A. I cannot.

Q. Then do you agree, or do you not, with the principle which has been followed in dealing with life insurance companies, where only the portion that is set aside for the shareholder is taxed for income purposes? Do you agree with that principle so far as it relates to life insurance companies? A. I have not given that any consideration.

Q. And you do not care to express an opinion?

A. No, not without consideration.

Q. You appreciate the principle that appears to underlie this application of income tax to life insurance operation?

A. I don't think I follow your question.

Q. I mean, do you appreciate the principle which they are seeking to apply in applying that formula? A. I do not know whether I appreciate it. I know what the statute says.

Q. You know what the statute says -- that is, with respect to the issuing of participating policies in life insurance, to the extent that the company sets aside, earmarks for the shareholders' account, the shareholder has no right or interest in respect to that amount; there is no income tax applying. A. I do not recall that as being the way the statute reads.

Q. Then how do you recall that the statute reads?

A. Well, we can look it up; but as I recall it, income tax applies with respect to life insurance on that portion appropriated to shareholders' account; it would make no difference whether it was participating insurance, term insurance or anything else -- that is not the test; the test

is what is appropriated to shareholders' account, as I recall it.

Q. Anything which is not appropriated to shareholders' account, which is part of the earnings of the life company, whether it arises out of surplus over losses and expenses or whether it arises by way of investment income, is not subject to income tax? A. Not unless it is appropriated to shareholders' account, yes.

Q. Now, you do not agree, or do you, that that would be a sound principle to apply in fire and casualty insurance -- that only the portion that is appropriated, that is lifted out of the policyholders' stream and set aside for another class of persons, the shareholders -- that that is the only portion that should be taxed?

A. I would not express an opinion on that. I have not considered it in relation to fire and casualty business.

Q. You went this far with me this morning: you said that so far as reserves that might be created for policyholders' account were concerned you believed they should be taxed? A. If the country is in need of money and that is a source of revenue, any reserves should be taxed, if necessity requires it.

Q. You are not recommending it as a sound principle of taxation? A. Oh, certainly not, because we are taxpayers and we have reserves.

Q. Instead of saying, "Well, we are subject to certain taxes, having regard to the fact that we are shareholders," have you ever given thought to the fact that you might either incorporate a mutual or issue participating policies; that the remedy lies in your own hands, to reduce your taxation?

A. Is it suggested that a joint stock company issuing participating fire and casualty policies now does not pay on those dividends?

Q. I am suggesting that to you? A. I do not know, but I hesitate to think that is correct.

Q. Then if you do not think that is correct, yet you may agree with the principle, since you have told me that you would be in favour of getting lower taxes, all things being equal; would it not be better, I am suggesting from your point of view, that you endeavour to clear that situation so that you would have the right to issue participating policies without being subject to the income tax, rather than saying to those who do issue participating policies that they should come into your group and be subject to tax? A. If we had thought that was the better approach under war conditions, we might have taken it. No, I do not think so at the moment.

Q. You say, "under war conditions." I take it that the most acute stage in the war condition, and the most acute stage as far as the operation of your business is concerned, was when the income taxes were increased so considerably back in 1941 and 1942? A. Correct.

Q. We are now in the year 1945, so the terms of war emergency that exist to support your answer will have to be related to conditions as they are now; is that right?

A. That is probably suggested in the proposition that taxes will go back to what they were in 1938, and I doubt if that is the fact.

Q. It is a matter of opinion? A. That is true.

Q. Then I am coming down to this question now. You are not suggesting in the use of the words "unfair competition," and "tax discrimination," which appear in various places in your brief, that when taxes were substantially increased in 1940 and 1941 your volume of business suffered, because you were subjected to higher taxes?

A. I would suggest this, from the figures in the Mutual Alliance brief, in appendix II; that the increase in volume over the year shown, which I think is 1926 --

Q. I am talking from the point of view of your company?

A. All companies increased 1.3 per cent, and the Mutual Alliance members increased 21.4 per cent.

Q. I am looking at your schedule C, in your main brief. I see that in the year 1940 your premiums were \$73,000,000 odd. Is that correct?

A. In 1940? Correct.

Q. Then in 1941 I see that they were \$84,986,000?

A. Correct.

Q. Then in 1942 they were \$82,913,000? A. Correct.

Q. And in 1943 they were \$84,538,000? A. Correct.

Q. So if I look at your intake, as represented by premium income, there has been no shrinkage; as a matter of fact there has been an increase during the period of these war years and heavy taxation?

A. That is correct. It

might not have been as great an increase as there otherwise would have been.

Q. Then I look at the underwriting profit which you report in each of those years, and I see that your underwriting profit in 1940 was \$5,422,000; in 1941 it was \$5,282,000 and in 1942 it was \$5,907,000. In 1943 it was \$3,575,000?

A. That is correct.

Q. Then your premium income increased for those years;

and in some of the years you had an increased underwriting profit, while in 1943 your underwriting profit was about a million and a half less than in 1942. That is correct, is it not? A. Yes.

Q. During those years, generally speaking, did your rates increase or decrease? A. That is almost an impossible question to answer, because of necessity some rates go up, individual rates, and some would go down. But what the overall picture is, I could not make a statement on.

Q. If it were substantial either way you would be in a position to say Yes or No, would you not? A. No, I would not be able to .

Q. You would not? A. Not without consultation with the blue book figures, and then I would not be certain. They are very difficult to read, in the light of rate levels.

Q. Then as far as your competition from the Mutual Alliance group is concerned, it is not reflected in your premium income, is it? A. I cannot come to that conclusion.

Q. I take it that unfair competition would have the effect you suggest, do you not, of reducing your business, or reducing your rates, or both?

A. Or reducing a possible or probable gain. It does not necessarily have to reduce it; it might not expand as much as it would otherwise.

Q. Remember there is another factor we have not mentioned which was operating in that period of four years of high taxation. That is, generally speaking it was a period of increased cost of operation. Did you experience those at all? A. The same as any other corporation.

Q. So that would be an item contributing to a lessening

of your underwriting gain? A. Yes.

Q. So that by reason of the income tax and excess profits tax, and the increased commissions in those years, there was less left for the shareholders' account? A. I think that would be true.

Q. Did the policyholders' account suffer in any way by reason of that taxation, that increased taxation?

A. There is no such thing as a policyholders' account. Do you mean did it affect the rate?

Q. Did it affect the rate? A. It would affect the rate in this respect, that if you and I are agreed that reserves are necessary and essential, and if it is necessary to secure reserves that joint stock companies must secure them by surpluses, on which it is taxed -- in order to provide reserves this rate must contemplate the possibility of surpluses out of which to get reserves, so to that extent, indirectly, it would have an effect.

Q. If you maintained the same rates and the same reserves, in the event of increasing taxation the shareholder would have to get along with less? A. Yes, other things being equal.

Q. I was interested in an expression you used this morning. You agreed that if a company satisfied the requirements of strict mutuality, it should be exempt from income tax? A. Correct.

Q. Apparently there was the greatest difficulty in arriving at any understanding of what strict mutuality was. Were you talking about strict mutuality in theory, or were you being realistic about it? A. That would be a matter of opinion. I cited an example this morning, what I considered to be an example of strict mutuality.

Q. I understand you to say that if, for instance, a mutual company operated in this fashion, that premiums were received, the money maintained without investment

income of any kind, the losses and expenditures paid, and the balance returned to the policyholders, you would agree that that was a strictly mutual operation? A. It would seem to me to be a strictly mutual operation.

Q. Then if in those circumstances I interpose a corporation for the handling of those funds, would you still agree that the return would be a return of unused moneys and therefore there would still be no problem of income tax?

A. If it acted as agent for the people whose money it had the management of.

Q. If it acted as agent? A. Yes.

Q. That would be a matter of law, as to how you would construe that? A. I think so.

Q. Then do I understand you to say that if those moneys were received by way of premium and temporarily invested, and there was some income, then the character of the operation would cease to be strictly mutual? A. I think in fact that under section 4(g) that is the case.

Q. Under section 4(g) it is income of the corporation which inures to the profit of the members or of any member. How are you construing the word "profit" then; are you considering it as benefit, or taxable income in the sense in which profits must be used under the Income Tax Act?

A. I am treating it as benefit or profit in the normal use of the word.

Q. Whether or not it gets into the hands of the member; is that right? A. Yes.

Q. Whether it is actually received by the member or not? A. I do not think the mere physical possession of it would make any difference, if it is to his account.

Q. Do you pay income tax on the basis of what you might get, or what you do get? A. If you have the right to it.

Q. Then in the case with which we are dealing, that of foreign mutuals, where the investment income is not subject to income tax, do we need to pay any attention to investment income which they might have from the investment of surplus moneys?

A. If it is the principle that the investment income of foreign corporations should not be taxed, I think it should apply to mutuals the same as to joint stock companies.

Q. So in that case, as far as the foreign mutuals are concerned, their underwriting gain would not in those circumstances be, shall we say, "tainted" by the fact that there was some element of investment income?

A. I do not think I follow that question.

Q. Is not the question clear?

A. I do not know what you mean by "tainted".

Q. I put that in quotation marks.

A. That is what I thought.

Q. I thought you suggested that the sin of mutualism, that where they violated the tenets of mutuality, was when they dared to invest some of their proceeds and received income. But what difference does that make to our consideration of the problem if the income they get is not taxable income?

A. Not taxable income in the hands of the corporation? Because it affects its character.

Q. What difference does it make?

A. Well, you change the character, and it makes a difference.

Q. You are suggesting that even though that income is not subject to tax, it has changed the character of the mutual organization?

A. Yes.

Q. In your brief you say something about the common test of mutuality. Is that what you had in mind?

A. You had better refer me to the text, so I can see it.

Q. On page 11, near the top, you say:

"The common test of mutuality, that there must 'complete identity between contributors and participators' is not met by any mutual or reciprocal insurer in Canada --"

A. That is correct.

Q. What is that common test of mutuality? You want complete identity between the contributors and the participators? A. Yes.

Q. You mean that because a policyholder might go into the plan and conceivably acquire some interest in some part of the hold-back which represented a collection from a previous policyholder who had retired; and that in retiring from the plan he might leave something there for the one who succeeds him -- is that the element which you say takes away the complete identity that is necessary between the contributors and the participators? A. It is one of the elements.

Q. What other element is there? This is just on the question of the common test of mutuality. It is the only one you have stated in your paragraph? A. That is correct.

Q. So it must be the only one? A. Yes, it is the one stated as the common test of mutuality. That in my judgment is a test of mutuality.

Q. Are you not stating an impossible condition for the operation of insurance of any kind, that you must have a permanent group of contributors during the entire operation of the company, and that if one member retires or dies you should dissolve the cooperation and start all over again? That is the alternative, is it not?

A. It may be the alternative, but I cannot see that the responsibility upon me is to suggest a method whereby the members of the Mutual Alliance can maintain their mutuality

and thereby maintain a right to exemption from taxation. If it is impossible, then that is not my responsibility.

Q. On that basis, then, you are suggesting that whatever that small item which might be left by a retiring policyholder, and might accrue to the benefit of a succeeding policyholder, who in turn might do the same himself -- you are suggesting that this small element -- A. It may or may not be small.

Q. You are suggesting that this element, whose existence is uncertain, because loss may come in the meantime --

A. And it may not be small.

Q. I am talking only about the Mutual Alliance operation; and the figures which were produced show that over a period of fifteen years the holdback of thirteen companies amounted to two per cent, or \$776,000, while in the succeeding year \$530,000 of that disappeared in losses, additional losses. You would agree that a holdback over a period of fifteen years for thirteen companies, amounting to only \$250,000, is not a substantial amount? A. But the very fact --

Q. Would you answer that question and then make your explanation? A. The two per cent --

Q. But I am taking less now. I am saying that in the sixteenth year they had losses which reduced it to less than one per cent. Is that amount of holdback of such a character that you suggest there should still be the theoretical concern of insistence upon strict mutuality; or should we not be realistic about it in the day to day operation of an insurance business? A. I would say that if it is an amount of two per cent which thereby changes the character of that organization from one of mutuality, do you not get out of paying taxes?

Q. If the holdback has that effect? A. Yes.

Q. You are not suggesting that to the extent that your contributors remain the same the holdback in those circumstances and in relation to those contributors would affect the character of mutuality? A. I do not follow your question.

Q. To the extent that you have the same contributors from year to year, then your relationship to the holdback is an absolute relationship of the same contributors and the same participators? A. Yes.

Q. To that extent you are not suggesting that there is not strict mutuality? A. No. If there is identity, then there is mutuality.

Q. But it is only when you have this change of policyholders in the stream that you suggest, whether it is large or small, whether it is fractional or very substantial, that it would change the whole character of the operation?

A. It changes the character of the organization.

Q. I see. You do agree with me that it would be difficult, if not impossible, to envisage the operation of an insurance business in the world as it is carried on to-day, without that change in your policyholders and therefore in your contributors and participators from year to year?

A. I have not attempted to visualize it.

Q. After all, you have been in the insurance business for some time? A. Yes, but I do not visualize what can happen to a joint stock company.

Q. Your policyholders change from year to year?

A. True; but we do not claim to be a mutual.

Q. Perhaps that is the answer? A. I think that is the answer.

Q. I say perhaps that is the answer to your problems of discrimination and unfair competition?

A. I do not think we need to get on the theory as to which philosophical outlook is the sound one as between joint stock operation or mutual operation.

Q. No, but I am trying to get on a very realistic basis as to what is the day to day and year to year experience in the operation of an insurance business, whether it is mutual or stock, and you have a changing stream of policyholders, have you not? A. Yes, certainly.

Q. One other question. Apart from the shareholders' interest is there any element in the rates which a joint stock insurance company may charge which would differ from the build-up of rates in a mutual operation? A. I cannot say anything on that. I know how we make our rates --

Q. I am not asking you that. I am asking you is there any element of difference, other than the shareholders' interest, represented by the underwriting profit, that item of two and a half per cent to which you referred --.

A. Not knowing how mutual companies make their rates, I could not answer that.

Q. Could you conceive of any? A. I do not think I can even answer that.

Q. Then let us go at it in this way. You say you put in your rate a two and a half per cent underwriting profit? A. I do not think I said that.

Q. Either you said it or Mr. Mann said it, and I take it you are speaking collectively.

MR. MANN: I did not say that.

THE WITNESS: It was in the quotation from the Masten inquiry.

BY MR. HAYDEN:

Q. No, the statement was made here that you had a two and a half per cent underwriting profit in your rate.

A. I did not make any such statement.

MR. MANN: I did not make any such statement. That is the quotation from the inquiry.

BY MR. HAYDEN:

Q. Is that your aim, in the companies which you represent? A. Oh, roughly speaking.

Q. The actual rate, as I calculated it on the figures you have given in schedule C, would run from 7.3 per cent to perhaps something over 5 per cent; that is your underwriting gain in relation to your premium income. A. I think we have placed an exhibit in our supplementary brief as to just what it has been over periods of ten years.

Q. I look at the figures for the year 1940 and see that the joint stock company premium income was \$73,000,000 odd, while the underwriting profit was \$5,422,000. Then I do my arithmetic, and it works out at 7.3 per cent?

A. That is so.

Q. Naturally if you were making provision in your rate for underwriting profit, the amount you would provide would be a gross amount? A. Oh, yes.

Q. Which undoubtedly would be intended to make provision for taxes? A. Yes. Some companies may earn more and others may earn less. Some will operate at a loss in any year, and others will make a bigger profit.

MR. HAYDEN: That is all, thank you.

BY MR. MANN:

Q. There is just one short question I should like to ask, flowing from this examination. Senator Hayden referred to schedule C, showing the increase in premiums and in underwriting profits of joint stock companies. Are you aware that in the years following 1940, namely 1940 and 1941, there was a very substantial increase in three-year business?

A. Yes, that is a fact.

Q. And the three-year business would be represented by a three-year premium paid in one year? A. That is correct.

Q. Which would be reflected in those figures?

A. Yes. There was an amendment to the statutes in most of the provinces, which had hitherto prohibited the writing of manufacturing and mercantile risks for more than one year. That provision was removed, with the result that in 1940 and following there was a big influx of three-year business at higher rates. That would appear in the income of that year, but it was for a term of three years.

Q. And it continued on into 1942? A. Yes. As policies expired, they were taken out on the three-year basis.

Q. And to some extent at least this was the reason for the figures, which looked like an increase in business?

A. It was a substantial amount.

Q. This almost seems to be a matter of argument, but I might put this one question to you. My learned friend gave you an analogy between life insurance on the one hand and fire, automobile and casualty insurance on the other hand. It may be fair to put the commission right on this. Life insurance cannot be cancelled by the insurer? A. I understand that to be a fact.

Q. Life insurance always becomes a claim, except in one event; that is, in the event of the insured failing to pay his premiums? A. Yes.

Q. It becomes a claim either in the form of the cash surrender value of the policy, or upon the death of the insured? A. Yes.

BY MR. HAYDEN:

Q. Did I understand you to refer to this heading in

schedule C? Is that premium earned or premium income?

A. That is net premium income.

Q. Suppose you had three-year business; what amount of premium would you take into the one year? A. The whole thing.

Q. You earned the entire premium income in one year?

A. For the purposes of the figure as put in the blue book, it is cash in, in the year. As far as reserves are concerned, they are put up over the period. You only earn those reserves down with the effluxion of time.

Q. That would be reflected in your underwriting gain, then, would it not? A. No.

Q. Where did you get the money to set up your unearned premium reserve? A. Out of the premium.

Q. Then this is a net premium amount. Would you not lift the amount for reserves out of that? A. No.

Q. Where does it come from? A. From the policyholder.

Q. If you include the premium for a three-year policy in your premium income for the year, then you set up an unearned premium reserve? A. That is right.

Q. Where does the money come from? A. Out of the premiums. But it is not the premium reserve in these figures; that is in fact premium income, whether it is for three years or twenty years.

Q. Then you pay your income tax on a net premium basis, do you? A. No, that has not anything to do with it. These figures here give you the net premiums.

Q. Let me put it in this way. This represents written premium income? A. That is right.

Q. And there is no statement in schedule C of earned premium income? A. No.

Q. On which basis do you pay your income taxes, or do you calculate them?

A. I could not answer that, because I do not fill out the forms, and I do not know anything about them.

BY MR. GRAY:

Q. Mr. Ham, how long have you been manager of the Canadian Underwriters Association of Montreal? A. Just under ten years.

Q. And prior to that time, I am informed, you were manager of an insurance company in Winnipeg? A. That is correct.

Q. For how long? A. From March, 1929, to 1935.

Q. About six years? A. About six years.

Q. So you have occupied a position, a managerial position, in the casualty insurance business for many years?

A. A branch managerial position.

Q. Have you brought with you a list of the companies referred to in your statement of representation, that is to say the 227 stock companies mentioned? A. Yes; I have such a list.

Q. May I have it, to put in as an exhibit?

A. Yes, sir.

Q. Is there anything in this list to indicate which of these are the 167 members of the Canadian Underwriters Association? A. No, there would be nothing on that list to indicate that.

Q. Have you brought with you a list of the 167 members?

A. I have not, but I would be glad to supply it to the commission.

Q. Then perhaps by just putting an asterisk opposite these names you could indicate which of the companies in this list are members of the Underwriters Association?

A. You mean now?

Q. No, not now but later. Would you do that?

A. Yes.

Q. Put an asterisk at the left hand side of the name of

the company to show the 167 companies who are members of the Canadian Underwriters Association; and I wonder if you would help us still further by indicating, with a distinguishing mark, the identity of the 88 companies which you say are particularly represented in your presentation, as a committee?

A. Yes, I can do that.

Q. Thank you very much. In your brief I think I remember that you adopted the argument of the income tax payers' association main brief, filed with this commission, insofar as it relates to the insurance business. Is that correct?

A. I think that is correct.

Q. What would you say is the relationship of the companies in this list just filed to that income tax payers' association, if any?

A. None whatever.

Q. Are these companies members of that association?

A. They may be, but I do not know of any that are.

Q. And is the Canadian Underwriters Association as such a member of the income tax payers' association?

A. It is not.

Q. Is any association with which you are officially connected either a member of or a contributor to the funds of the income tax payers' association?

A. Not to my knowledge, and I do not believe it to be so.

Q. Reference was made at the opening to the report of the late Mr. Justice Masten in Ontario, in 1919, and I want to ask just one or two questions about that. In the first place the 167 companies who are members of the Canadian Underwriters Association, were they or were they not substantially represented in the Canadian Fire Underwriters Association, which appeared before this commission in Ontario in 1919?

A. Substantially the same membership.

Q. And that is substantially the organization of which

you are now manager? A. Yes.

Q. And I take it, with regard to the opening submission of your counsel and also your evidence, that when you quote from this report, a part of it in support of your case, you are willing to adopt the whole report as having the same weight as that part you quoted? A. As far as I am concerned, yes.

Q. Referring just for a moment to the recommendations of that commission at page 40 of the report, I notice the first two are these:

"My suggestions and recommendations as embodied in this report, may be summarized as follows:

"1. Supervision and control by the province, of the Canadian Fire Underwriters Association, in the manner, and to the extent set forth on pages 22 and 23 of this report."

Was that recommendation ever implemented by legislation?

A. I believe it was. Perhaps you can confirm that, if I am wrong. I believe it was, in the province of Ontario, and I am not sure whether it was done anywhere else.

Q. My own information is to the contrary.

A. Enabling legislation was passed.

Q. How did it correspond to the supervision and control by the province of the association, as recommended by the commission? A. It depends on what you mean by control. They passed legislation, following the Masten report.

Q. But that did not embody, or did it, any measure of supervision and control by the province of the Canadian Fire Underwriters' Association? A. Yes; it brought in the right of inquiry. I am speaking from memory, and it is a long time since I looked at the statute.

Q. I have the statute here to which you refer. To shorten

it up let me put it in this way. There is a part here --

A. That is the statute to which I am referring.

Q. And I suggest it only required you to file a copy of your by-laws and amendments thereto from time to time, and that was the only measure of the active submission of your body to the legislative control. Am I right?

A. No, I do not think that is right. I think the statute speaks for itself.

Q. Let us not take any more time; but can you mention any matter of supervision and control recommended by Judge Masten which was included in the legislation? Can you name any measure of supervision and control? A. Well, for instance the superintendent has access to the books and can pursue inquiries. I am merely reading the side notes of the statute. The superintendent is empowered to order a rate adjustment, and he has authority to require information to be filed.

Q. Has he authority to order a rate adjustment? Is that in the act? A. It says:

"It shall be the duty of the superintendent, after due notice and after hearing before him, to order an adjustment of automobile rates whenever it is found by him that such rates are excessive, inadequate, unfairly discriminatory, or otherwise unreasonable."

But I think the statute speaks for itself.

Q. I did not intend to involve you in a discussion of the statute, but I will leave it in this way. The statute, of course, will speak for itself; but I thought you would agree with me if I said that the recommendations of the Masten report, in so far as they relate to supervision and control by the province, were not implemented in that legislation. It is filed, however, and it is a question of fact.

THE CHAIRMAN: The witness would appear to indicate that it does, whether or not it is carried into practice. I am sure I do not know that, but the wording would imply supervision.

MR. GRAY: If you will permit me to give a little evidence as a witness I would say to the best of my knowledge, understanding and belief the recommendations of the commission were not adopted. In lieu thereof the only legislation is that which is now found in that part of the Ontario Insurance Act to which we can easily refer. In substance it means merely that they must file their charters and by-laws and that there is the right of inquiry by the superintendent of insurance in certain cases, but not otherwise.

Q. Now with regard to the report itself and its findings, my learned friend Mr. Mann read a portion of the report. May I refer you now to page 11 of the report and ask you if you accept these findings as having equal weight. I will ask the reporter to copy into the record, if he will, the part of that page which begins with the second paragraph--

MR. PARKER: I do object, my lord, to having the record built up in that way. I suggest that the evidence in the record should be relevant evidence, and at the moment I cannot see how the question of whether and to what extent the Canadian Underwriters Association is controlled, or anything else, has anything to do with this inquiry.

THE CHAIRMAN: I fancy the report speaks for itself. We are not interested in dissecting it, but we will read it.

MR. GRAY: Then permit me to confine myself to two sentences, and to ask this witness a question regarding them. There is a reference on page 11 to the New England Mutuels. I want you to identify, if you will, the New

England mutuals referred to on that page with the factory mutual fire insurance companies who have made their submission to this commission.

MR. PARKER: I do not know that the witness should be called upon to construe the report.

MR. GRAY: It is not a question of construing the report; it is a mere question of fact.

Q. Are the New England mutuals referred to in this report, or are they not, the factory mutual fire insurance companies that have made their submission to this commission?

MR. PARKER: The witness could not possibly answer such a question in any court of law in this country.

THE CHAIRMAN: If you were in court, Mr. Gray, I would sustain the objection without hesitation, because the witness did not speak of that report; Mr. Mann spoke of it. It does not follow as a matter of cross-examination. However, we are not in court, so go ahead.

MR. GRAY: Certainly I would want to follow any indication of your wish in the matter, whether it were binding or not, of course; and I am not going to trespass further since you indicate that you do not think it is relevant. I will just keep myself within the bounds of what I think you intend. I should like to read these two sentences, which I intended to do, and then see if the witness has anything to say about it.

THE CHAIRMAN: Very good. Can you answer that question?

MR. GRAY: I am going to abandon the question to which objection has been taken, Mr. Chairman, in acknowledgment of Mr. Parker's objection. At page 11 of the report of the Masten commission I read:

"The third class of competition consists of unlicensed foreign companies, including foreign mutuals,

reciprocals and Lloyds. This is for the most part insurance which the insured himself procures directly, or through his brokers, in the United States, Great Britain, or other foreign parts. It largely consists of carefully selected risks, and is, in the majority of cases, insurance covering manufacturing plants. The New England mutuals insure none but sprinklered risks, and one feature of their work is the very special and valuable inspection which they continuously make of the properties insured. They have undoubtedly been very successful, and their action in Ontario has resulted in great reductions in the cost of insurance on sprinklered risks."

Do you think it is a fair question to ask this witness, Mr. Chairman, after referring to the Masten report, if he accepts that finding in the same way and with the same weight as the one his counsel quoted?

THE WITNESS : I would be most happy to accept it.

BY MR. GRAY:

Q. Then, here is another sentence, further down the page:

"My conclusion is that the non-tariff companies do yield appreciable competition, and that competition ought to be encouraged as a natural and proper method of reducing premiums, and that great care should be exercised in passing any legislation tending to lessen competition.

"I thus conclude that there exists in Ontario a combination of the principal insurance companies who largely control the rates of fire insurance, and that large lines of fire insurance can be secured only at the rates prescribed by that combination."

Do you accept that, Mr. Ham, as a valid conclusion?

A. I have appeared all week as counsel for non-tariff stock companies, and I do accept it.

Q. Thank you. Then on page 30 and following is a section of that report under the title "Unlicensed Insurance," and I simply call that to the attention of the commission and ask them if they will be good enough to note what is said there by the commissioner. That is on pages 30, 31, 32, and 33, down to the middle of the page ending with the words:

"On this phase of the inquiry I am not prepared to make any recommendation, but submit the facts as stated above for your information and consideration."

I want to ask you, Mr. Ham, whether at the time this report was made the companies that have appeared here, the reciprocals, the factory mutuals and the American Mutual Alliance, were, most if not all of them, doing unlicensed insurance, and whether they are the group referred to in the Masten report?

A. I would not be able to answer that, because I was not interested in insurance in 1918 to 1920.

Q. But you have been interested in the Masten report, have you not? A. Yes, as a report.

Q. Just be fair to us now, and let us hear what you say about that? A. I cannot make a statement as to who were the unlicensed insurers in Canada. There would be no record of them in 1918 to 1920. I would have no idea.

Q. Is it a fact that your association -- and when I say "your" please understand that I mean the Canadian Underwriters Association or the companies which compose it-- were before the Masten commission at that time asking, among other things, that a tax be placed on these unlicensed insurance companies or on this unlicensed insurance, against every person who sought to insure property in these companies? A. It might be. I could not answer that.

Q. Mr. Ham, this is your association, and that is the report which you have cited. Can you not say whether or not that is a fact? A. I cannot. It is not within my knowledge.

Q. I wanted to ask another question, but perhaps you will not be able to help me in it. I wanted to ask you this with regard to the case that was then made for a tax on unlicensed insurance in these companies. There was no element in there of service by the state to support your application, and by "your" I mean the association, for the taxing of these premiums, was there? A. No what?

Q. No element of service by the state to justify a tax on unlicensed insurance, to the provincial treasury; or was there? A. Will you restate the question? I want to answer it if I can, but I cannot follow it.

Q. I will change it, then. This morning in making your statement you said there should be equality of taxation between these various groups of insurers because of their similar position under government, and the service of government that they receive. Am I right? A. That was stated. I do not know whether I said it.

MR. MANN: I said it.

BY MR. GRAY:

Q. Well then, I am asking you whether, when your companies made a similar submission seeking the taxation of these same premiums in similar companies, there was any such element to support your demand?

A. I would not know that either.

Q. If they were unlicensed would you not know? If they were not in Canada at all? A. If they were not in Canada and had no rights, then of course there would be no element of protection of the state. That is self-evident.

Q. But that consideration did not at all prevent the stock companies who are here to-day from urging taxation of the premiums at that time?

A. Apparently it did not, because they urge it.

Q. I am suggesting to you that really your position is no different to-day than it was in 1919, and I want you to comment on this. Just as in 1919 you sought to restrain unlicensed insurance by taxation, in the submissions you made to that commission, so to-day you are seeking to restrain similar competition by a new imposition of tax; and that is your real purpose. What do you say to that? A. I say that is not the fact.

Q. Very well. Let us recall the attitude that your companies took on these four occasions, and I will just mention them. There was the attempt of Montreal Brokers to carry on business on behalf of Lloyds, in Montreal, which brought forth the insurance reference in 1916. Do you know about that? A. I know nothing about it, except having read the reference.

Q. You know that your companies were there involved in that litigation, and went all the way to the privy council with it? A. I do not know that. I presume perhaps they were; I do not know.

Q. It is in the record. They were there.

A. If it is in the record, the record speaks. I do not know; I was not in the business at that time.

Q. Then on that occasion, and in 1923, and in 1931, and in 1942, the companies which you represent here to-day were all represented in an effort to maintain legislation which excluded these companies from the privilege of carrying on business under license in Canada. Is that right?

MR. PARKER: I think I would be derelict in my duty

as counsel for the commission if I let the record continue further without at least speaking. I cannot see how the history of the dispute between these two groups of companies through the years has anything to do with this matter before the commission. If the commission feel they would like to hear about it, I will not make any further objection, but I say I feel it is my plain duty to try to restrict the record to some proper limitations.

THE CHAIRMAN: I am afraid I cannot see the relevance, Mr. Gray.

MR. GRAY: Very well, then; I will not pursue it, Mr. Chairman.

Q. The next question may be open to a somewhat similar objection, so before you answer it, Mr. Ham, I will ask you to wait for my learned friend Mr. Parker to state the objection, if he has one.

MR. PARKER: If the question is in the same category, why do you not decide it yourself and not ask it?

MR. GRAY: I do not think I can decide it. I want to ask this witness if he could give us any explanation or any factual information to help us understand why the mutual fire companies are here in this inquiry and why the life insurance mutuals, governed by the same law and the same subsection, are not here or under attack?

MR. PARKER: I suggest that is just so much more objectionable.

THE CHAIRMAN: I do not need an objection from Mr. Parker in that connection. It is the choice of the minister, in preparing the terms of the reference.

MR. GRAY: I could not find anything in the order in council about it. I do not find a word in this order in council.

MR. PARKER: You know why the factory mutuals are here. You do not have to ask the witness that question.

MR. GRAY: I have not asked him yet.

THE CHAIRMAN: Certainly if I were a witness in the box I would say, "I cannot answer that question," and he would be perfectly justified.

MR. GRAY: He would be perfectly right and true in saying it, but I happen to think this witness would not be able to say that, because I think he had an active part in the proceeding.

MR. MANN: An active part in what? This is getting serious.

THE CHAIRMAN: I would suggest that the witness answer the question. As I said before, if this were in court I would maintain the objection, absolutely.

MR. GRAY: Then please do not let me go on with it if you do not think it should be there.

THE WITNESS: I will be glad to answer the question. I do not know why the mutual life companies are not before this commission, or any life companies.

MR. GRAY: Of course that ends it, then.

Q. Now, Mr. Ham, reference has been made to certain reciprocal agreements respecting the taxation of income arising in Canada and in other countries to corporations which do business in more than one country. To what specific agreements does your testimony refer?

A. I think my testimony was that I presumed there were such agreements. I have never seen them, but undoubtedly the Department of Finance would have that evidence. I do not know if they are in existence. It was presumption on my part.

Q. So you are not able to help me or the commission

with reference to any particular convention? A. Oh, no; certainly not.

Q. I should like to call your attention, and the attention of the commission, to the reciprocal tax convention which is published as part of this 1943 edition of the Income War Tax Act. It is also in the 1944 edition. This was executed at Washington in 1942.

MR. PARKER: When was it ratified?

MR. MANN: June 15, 1942.

BY.MR. GRAY:

Q. At any rate there is no doubt about the ratification. It was agreed to on March 4, 1942. That is the only reciprocal tax convention that I know of to which your testimony could refer; but if there is any other I would be obliged to you if at some later time you would let us know what it is? A. I am sorry. When I made the reference I did not even know that this one existed, in the back of my copy of the Income War Tax Act. It was pure presumption that there was any such agreement.

Q. It seems to me so important that I should like to ask another question; whether or not you are able to answer it remains to be seen. In that tax convention the only paragraph which I find that could have any relevance to this inquiry is paragraph (4) of article 3:

"To facilitate the determination of industrial and commercial profits allocable to the permanent establishment, the competent authorities of the contracting states may consult together with a view to the adoption of uniform rules of allocation on such profits."

I want to ask you whether you can tell the commission whether any use is being made of that power which would affect the

subject matter of this inquiry? A. On that question I would have no information at all, sir.

Q. Then I suggest that in the absence of any other information, it seems that we ought to proceed as if there was no agreement between Canada and the United States, or between Canada and Great Britain, which affects the allocation of investment income of British and foreign stock companies for taxation purposes. Is that right?

MR. MANN: I take it the commission will examine into the late 1944 discussions between the British government and the Canadian government, which probably will be available.

+ THE CHAIRMAN: We will look into that, Mr. Gray.

MR. MANN: There was an exchange of communications between his Majesty's government in Great Britain and the Canadian government.

BY MR. GRAY:

Q. Then as far as we are concerned, with the material before us, I continue my examination as if there was no effective agreement between Canada and any other country affecting the allocation of insurance company profits. Was there or was there not, to your knowledge, an arrangement made by the British and foreign joint stock companies, acting collectively, with the Canadian tax office which produced a special or particular formula for the ascertainment of taxable income? A. If there was I had nothing to do with it and I know nothing of it.

Q. Do I understand you to say, then, that you do not know of your own knowledge whether or not such an arrangement exists? A. That is correct.

Q. And so, of course, cannot explain it if there is one? A. No.

Q. Are you able to help us on this. I think your brief says that you wish to recommend to this commission the adoption of the principles of the legislation in the United Kingdom in relation to the mutual insurance business done in Great Britain. Is that what you are recommending to this commission?

A. The recommendation is:

"that the commission recommend that the administration of these measures be brought in so far as possible into harmony with the provisions of the administrative sections of the income tax and corporation profits tax branches of the British legislation."

Q. In order to ascertain just what that means, do you mean that you wish to have this commission recommend for application to factory mutual companies in Canada a formula for taxable income similar to that applied in the United Kingdom?

A. That is talking about administrative practice.

Q. But I asked you a different question. Do you wish to have the question read?

A. No, that recommendation does not compass that, does not mean that.

Q. Then if the United Kingdom allows mutual insurers to deduct, as an item of expense, their disbursements to policyholders by way of dividend, do you agree that a similar rule should be adopted and applied in Canada?

A. No.

Q. Then what rule do you say should be applied to the treatment of repayments to policyholders by way of dividend or refund?

A. What rule?

Q. Yes, what rule? Do you want to tax it or not?

A. Yes, want to tax it as premium.

Q. Even though it is not done in the United Kingdom, you want it done in Canada? A. Correct.

Q. I think you know that in the United States such deductions are allowed in the ascertainment of taxable income under all formulae acquired there? A. I do not know whether that is so under all, but I accept that; I imagine it is correct.

Q. So really, then, your brief must mean this; that you are striking out on a new line, and you want something done in Canada that is done neither in the United Kingdom nor in the United States. Is that right?

A. The brief speaks for itself. We want the dividends, the consideration, considered as premium. That may be different in the United States; it may be different in England.

Q. Even though it is not done in the United Kingdom and is not done in the United States? A. If it is not done in either place, we would still recommend it.

Q. Do you know of any taxing jurisdiction in the world where the rule you propose is applied now?

A. I do not know of any.

Q. Then is there any other element in the factory mutual balance sheet which you say shows an income which ought to be taxed, in addition to this refund to policyholders? A. Yes.

Q. What is it? A. Any penalties they might exact upon cancellation of a policy or membership. Reinsurance premiums with other insurance companies. Investment income.

Q. I presume that would also appear in the premium account and be taken up in the ordinary ascertainment of net premiums? A. I would not be able to tell you how the mutuals do it.

Q. You could not imagine any premium account which did not take care of that, could you? A. Whose premium account?

Q. Anybody's; any insurance company's premium account, anywhere? A. Well, just a minute. Investment income would not be in the premium account?

Q. I said the premium account? A. I mentioned four or five items. You asked if they would not all appear in the premium account. Penalties do, I assume.

Q. You call them penalties. I have never heard the word used in that connection before. Have you heard it elsewhere?

A. It may be a misinterpretation of the word, but to me it is a penalty.

Q. Never mind what you call it. Cancellation refunds go into the ordinary insurance company's premium account? A. That is correct.

Q. So it would be there. Then outside of the premium accounts what if any part of the income of the factory mutual companies do you recommend this commission to find should be taxed? A. If the foreign companies are to be exempt on investment account, I think that should apply to factory mutuals, and only the premium account would be considered.

Q. You have looked at the factory mutual material which has been filed here; you have had it before you, so perhaps you can answer this question. If you eliminated investment income from the factory mutual account, and took only the balance of their premium account and called that taxable underwriting profit, could you find any substantial amount whatever to tax? A. The allocation in the brief of the factory mutuals indicates that you would not, but I

do not know.

Q. That is the submission of the factory mutuals, that you would not find anything that would produce any substantial income whatever. Are you able to give any contradictory evidence on that point?

A. I certainly am not.

Q. Then it would appear to the commission, if they had to judge this matter on the evidence that is in, that the taxation of the factory mutuals on the underwriting account as it is now made up, would produce no substantial amount of tax revenue. Is that right?

A. That depends upon how the bookkeeping is done in the factory mutuals. I do not know.

Q. You are not able to help the commission by suggesting--

A. If I could I would be very glad to do so.

Q. Then one other question, somewhat along that line, but I think it is a little different. Evidence has been given by Mr. Freeman that for the twelve months ending March, 1945, there was retained by the company out of moneys available for distribution to policyholders a certain item which he said was 1.42 per cent of the premium deposits, which he said went into the reserve. Do you think that item so held back ought to be included as a taxable item in any application of this Income War Tax Act to factory mutuals?

A. You will have to give me a better description of what 1.42 per cent is.

Q. Let me put it in this way. A. That is what goes to reserve, is it?

Q. Let me put it in this way. The factory mutual makes up its account for a twelve months' period, and it has certain income and outgo. That shows that there is

available, that is there remains from the premium deposit received at the beginning of the twelve months, .93.49 per cent of the premium deposit, and they decide to return only 92.0 per cent to the policy holder, which means that they reserve in the hands of the treasury of the company 1.49 per cent of the premium deposit. That was the evidence given yesterday. Are you suggesting that this ought to be the subject matter of tax, to be applied under the Income War Tax Act? A. If it is income it should be taxed.

Q. Is it or is it not taxable income? A. I am not interpreting that.

Q. I thought you might want to say something about that; that is the only reason I raised the point. I am not sure whether this next question will be of any help, but I will ask it anyway. The information filed with this commission yesterday shows that at the end of 1938, for the twelve months' period 88.60 per cent of the premium deposit was available for return, but 94 per cent was paid back to the policyholders. In other words, although because of unfortunate experience in that year of 1938 -- that was the year of the hurricane -- they had left only 88.6 per cent of the premium deposit they paid to their policyholders 94 per cent.

MR. PARKER: No. That is an absolutely impossible thing mathematically. It would be impossible to pay back 94 per cent. They may have paid an amount out of some other fund equivalent to 94 per cent.

THE CHAIRMAN: They evidently made a loss to that extent.

MR. GRAY: Yes, my lord.

THE CHAIRMAN: That is not paying back, then.

MR. GRAY: Actually they did pay back.

THE CHAIRMAN: It must have been paid out of other funds in their hands.

MR. GRAY: I would still maintain, with great respect, that it is paying back; for this reason, that what they did obviously was to draw upon their reserve account, to the extent of something over \$1,000,000.

THE CHAIRMAN: That is another fund; that is from accumulated reserves, I take it?

MR. GRAY: Yes, but they put that into their current account and then, having satisfied all their liabilities --

THE CHAIRMAN: If you will say that they paid it, but not that they paid it back.

MR. GRAY: Very good, sir; I will be glad to make that amendment. The fact I am trying to bring to the attention of the witness is this, and I think it is independent of that difference in terminology.

Q. With the deficiency in 1938 of 88.6 per cent, and the payment of 94 per cent, there is a difference of 5.4 per cent. The surplus in March 1945 was 1.42 per cent. I want to know from this witness whether, putting those two facts together would affect his judgment as to whether this annual addition to reserves, when it occurs, is properly a taxable item? A. When you say "paid back" is it actually paid back or is it merely just a book entry?

Q. It is paid back if the policy is terminated. Presuming the policy is terminated at the end of the year, it is actually paid back in cash. See if you can be of any help to the commission in your submission as to how the taxing officer should deal with that situation, in the application of the Income War Tax Act? A. I cannot answer it. If it is in income it should be taxed; if it is not -- I cannot follow the method of accounting of the factory mutuals.

Q. So far all I have got clearly as to your position is that you want so-called dividends or reimbursements of the premium deposits taxed. Now, what other element, if any, in the factory mutuals? A. Any other element of income. And if it is a fact that foreign companies are not taxed on investment income, I do not see why factory mutuals, being foreign companies, should be taxed. If it turns out the other way ---

Q. That just leaves it as a generalization. A. Yes.

Q. You gave us some figures this morning with respect to factory mutuals which I have not yet seen. Have you got them with you? A. Here they are.

Q. This is an exhibit which you produce showing the factory mutuals Canadian business from 1936 to 1943, inclusive, and it shows net premiums written and net losses incurred, and losses charged to Canada. A. You possibly may not understand that reference; it has reference to a paragraph in your brief.

Q. I think I understand it. The loss charged to Canada is 7 per cent of the total loss for that period, and you produce an excess of the actual loss incurred -- no, in excess of the amount charged to Canadian members over the actual loss which physically occurred in Canada. What conclusion do you wish this Commission to draw from those figures? A. The only conclusion I would think could be drawn, or that I would put before the Commission, is that in that period, whatever your rates might be, they absorbed a loss of \$1,500,000 of actual Canadian loss. Applying the formula of 7 per cent of total loss to the figure of total loss for factory mutuals in the United States and Canada, it produces a charge on your books

against Canadian business of \$1,500,000 as against actual Canadian loss of \$1,100,000. That leaves an actual charge against Canadian business of \$384,000 in excess of actual Canadian loss.

Q. May I put my question this way: to put it colloquially, so what? A. So that.

Q. So what? What do you wish them to conclude from that? A. They can draw their own conclusions from that.

Q. We would like to have your opinion. What do you conclude from that? A. What those figures show is my conclusion. The significance of them may mean one thing to you and may mean another thing to someone else, or to me.

Q. Tell me their significance to you? A. The significance to me is that when Canadian business, as such, receives so much in premiums, and paid out so much in losses, it must mean something. That is the Canadian operation of those companies. But with respect to the books of the factory mutuals, by applying that formula, there is charged to the Canadian policy holders \$384,000 in excess.

Q. And may I take it you approve our formula to distribute the loss proportionately among our membership?

A. It depends upon what purpose it is distributed for.

Q. For the operation of the company. You do not think that is a wrong thing to do -- or do you?

A. I do not presume to give you advice.

Q. Am I to assume that that is the advice you are giving the Commission? A. The Canadian business should stand on its own feet, as Canadian business.

Q. Is that what you wish the Commission to believe from this formula? A. There was no ulterior motive,

I can assure you, in what I said.

Q. I want only the obvious answer, with no reference to the ulterior. What do you suggest the Commission should think about that? A. They can see what effect the formula you suggest has on the actual Canadian operations of the companies in Canada.

Q. In other words, you wish them to think this, that in the period with which you are concerned, that is a period of four years, 7 per cent of the business located in Canada contributed more in premiums proportionately than it did in loss? A. Yes, and another four years, possibly the next four years, might show the reverse.

Q. Precisely. So what? So far as the Commission is concerned, how are they to apply that information? Then, you referred to the fact in your evidence with respect to mutuals -- and I suppose you meant factory mutuals doing business by way of re-insurance with their other companies? A. Yes, I meant mutual companies, generally -- factory mutuals and others.

Q. What conclusion did you wish the Commission to draw from that submission? A. I know the name of the Manufacturers; and what is the name of the other one in the group?

Q. The What Cheer Mutual Fire Insurance Company. A. My suggestion is that a re-insurance transaction between Manufacturers Insurance Mutual Company and the What Cheer Insurance Company is a transaction with people other than members out of which venture a profit may be made for the benefit of either of the companies.

Q. Have you looked at the policy which was issued? A. I was not supplied with a policy.

Q. Where do you find the "non-member" with whom

they are doing business? Who is the non-member?

A. The other insurance company.

Q. I am afraid you have not looked at the contract or heard Mr. Freeman's evidence, or that you did not understand it, because I think he made it clear -- made two things clear, which I shall place before you. I would like you to criticize what I have to say, if you wish, because I am going to say that Mr. Freeman's testimony, as I understood it, definitely showed this, first, that the placing company had no profits of any sort arising from this re-insurance, because it returned to the insured business the full amount that it received from the re-insuring company, both in relation to loss and return of premium. That is the first point he made.

A. Well, with respect ---

Q. And no profit; you do not dispute that, do you?

A. I do not dispute it; but it does not get us anywhere.

Q. My point was this, that the insured had a direct right of action against the insuring company, in his contract, and was by virtue of the contract a member of the re-insuring company. Did you get that? A. I did not get that explanation, either.

Q. Then, assuming that that is the fact, what becomes of your point in relation to the factory mutuals?

A. If, of course, What Cheer becomes ipso facto a member of the Manufacturers Mutual Insurance Company, immediately upon getting a policy from them, then of course there is no point at all.

Q. Of course not. Actually it is quite different from that. If he insures the XYZ manufacturing company he is, by virtue of that contract, a member of each of the individual re-insuring companies. A. Of course,

in order to place a construction upon that I would have to see the policy.

Q. Well then, we will have to leave it at that. But I call the attention of the witness and the Commission to the fact that whether or not Mr. Ham's point and argument is properly applied to others, the nature of the transaction applied to the factory mutual fire insurance company.

Then, one other thing about these figures: in your supplementary brief, referring particularly to exhibits B and C, you have given premium figures for the factory mutual companies in the left-hand column on both pages. I object to the figures you have given, and I say that they are incorrect and misleading on the basis of testimony already given. Therefore I should like to read the correct figures into the record so that the Commission will not be misled by this exhibit. A. Well, it should be noted that the figures are blue book figures, of course. Your complaint, I understand, is not against my tabulation, but against the figures which are supplied by the blue book.

THE CHAIRMAN: Of course the way to do it would be to put a witness in the box to make the correction. You may state the correction, and that is as far as it will go.

MR. GRAY: I shall do it shortly, and I would ask the reporter to take these figures down as being the correct ones for 1943, in Exhibit C. These are the figures:

The Arkwright	-	\$ 199,311
The Blackstone	-	259,472
The Boston	-	239,288
The Cotton & Woollen		129,201
The Fall River		61,645

The Firemen's Mutual	\$	190,491
Manufacturers Mutual		841,861
Philadelphia Manufacturer		77,379
The Protection Mutual		82,304
The What Cheer		125,332
The Worcester		57,053

You will observe that those figures are anywhere from double to treble the amount you have here.

MR. MANN: What is the total?

MR. GRAY: I have not totalled it.

BY MR. GRAY:

Q. They are double to treble the amount cited in your exhibit, and I would simply say that although I have not the figures for 1938 relating to exhibit B, I am quite confident a similar variation would be found in that respect. If you adopt the figures I have given you as correct, what conclusion can the Commission draw from exhibit C? A. Well, if they are doubled or trebled in premium, and the tax figures remain the same, and the expense figures remain the same, relative to the premiums there has been less tax and less expense percentage-wise.

Q. And, of course, the comparison falls down with the other companies at once, does it not? A. Yes, quite.

Q. So that the comparison goes out the window. And what conclusion do you wish the Commission to draw from the factory mutuals' exhibit? A. I would like to have the opportunity of supplying approximate figures for different companies to compare with your figures, which you have just supplied so we will see what the result is with comparable joint stock companies reaching volumes nearest approximating the companies and figures you have just given.

Q. Yes. Then, one further question and I shall have finished. At page two of your main brief you have set forth a description of the types of mutual insurance and in A described as "mutuals operated in accordance with the principles of mutuality" I notice that paragraph two is the section under which factory mutuals ought properly to be included, in your classification. A. Not in my judgment, sir.

Q. Where would you put them? A. I would not put them in that classification, at all -- in any of the classifications.

Q. You would not put them in any of these classifications? A. No.

Q. Not even under the so-called mutuals with taxable income? A. Oh, yes, I was looking at the first three. Yes, they would come under the so-called mutuals with taxable income.

Q. Which division? A. I would have to read them over. Certainly it would not be the first one, because you are not organized under provincial insurance acts. Then, it would not be under the second one, either, or the fourth or the fifth. They would come under C, foreign mutuals, where it states:

"Foreign mutual insurers may operate on any of the bases mentioned above or variations of them."

So, under that particular classification we can put factory mutuals.

Q. You have not attempted to describe them, at all? A. That is correct.

Q. We are just miscellaneous. A. Yes.

Q. I suggest that we would come properly under A (2), according to the words you use in that section.

A. I cannot accept your suggestion.

Q. Why not? What is there that distinguishes us from the companies in A (2)? A. Because the member has only a right with respect to the fund, but not a right to it.

Q. Where do you find those words in A (2)?

A. You have asked for the distinction.

Q. I do not see anything like that in A (2).

A. It is not there.

Q. Let me read A (2). A. That is the reason you do not get in there.

Q. I do not see those words anywhere else. A (2) states:

"A B and C may incorporate and the corporation may act as a medium to incur the necessary expenses for operation and to collect contributions from A, B and C to a common fund."

Is that not the factory mutual fire insurance companies?

A. A short description of them, yes. Yes, they might get within those words. I can assure you you were not intended to be within them, and I do not think you are within that group of true mutuality.

Q. Well, we will leave it there, with this suggestion, that those are the only words I can find in your analysis which seem to be descriptive of our operations.

BY MR. MASON:

Q. The hour is getting late, and I shall be extremely brief.

THE CHAIRMAN: It seems to me that with all the good will in the world we will not be able to finish tonight. If Mr. Ham is examined further, and Mr. Hurry is examined at some length, we will not be able to finish today, and

we will have to impinge on our administrative period on Saturday, with a view to continuing tomorrow morning. That is all we can do. Unfortunately, Mr. Nadeau was called to Montreal, and will not be here, but we will do the best we can. That being so, we might finish with this witness now, and then adjourn.

MR. MASON: While I intend to be very brief, I do not wish that to be taken as an indication that I would not like to take longer. There are many things I should like to cover, but I shall refrain from that temptation.

BY MR. MASON:

Q. Will you please look at page eleven of your first brief. I listened with great care to the explanations you have given to my learned friend Mr. Parker, and to the Commissioners, as to the meaning of paragraph B at page eleven. I must ask you now to enlighten me further upon it. Perhaps I am so tired I did not understand your answers properly, but I should like to know definitely what paragraph B means.

But, first of all, I would ask you if you have made a careful study of the subscribers' agreement that is a portion of the brief for the American Reciprocal Association? A. Yes, I have read it, since I received your brief.

Q. Looking at paragraph B, I want to put certain simple questions to you, the first of which is this: supposing in a given year a subscriber to an exchange paid \$10,000, and that \$5,000 of that was consumed as his share of losses and expenses, and that \$4,000 was put to the credit of his reserve account, and the remaining \$1,000 was returned to him in cash, in the ensuing year what taxation would you levy upon that subscriber,

if you applied the principles which you are enunciating here? A. I do not think I am enunciating any principles of taxation, except the broad one that among competitors the tax should be on a comparable basis. My reply to you with respect to that is that if (A) takes \$10,000 and puts it into a fund to be self insured he must have earned more than \$10,000 if he had a taxable profit, because he must pay tax on his profit. So he is taxed on that. He puts \$10,000 into a special account as a self insurer. That \$10,000 may earn income. On the income the self insured is again taxed as part of his actual income. You say the reciprocals are self insurers. By taking \$10,000 and putting it with the attorney-in-fact (A) is able to set up \$10,000 as an expense for insurance. When he gets credit back I suppose he reduces the expense item by the amount of the credit. But that fund, because of the introduction of the attorney-in-fact, comes back as an expense; whereas if he built the fund himself he would be taxed to get it, and pay taxes on the earnings of it.

Q. And, having given me that, would you mind answering my question? I have asked that, because I do wish to understand what you mean in paragraph B. Tell me how you would tax that man in the circumstances I have outlined.

A. I have not evolved a theory on taxation.

Q. You say --

"The tax on income and profits in respect of unincorporated bodies such as reciprocal exchanges and inter-insurers who act through an attorney-in-fact, be assessed to income tax upon the respective member."

In my supposed case, how much will you assess under that category? A. As yet I have not had the job given me

of drafting the taxation statutes, so I cannot tell you that.

Q. Then, you do not know what this means, do you?

A. I say the income should be taxable.

Q. Do you know what it means; do you know what your proposal means when you carry it into effect? A. I have not carried it into effect.

Q. You are saying to the Commission that this should be done, and I am asking you, before the Commission, what you are suggesting they should do, and with that in mind I have given you a concrete case. I should like to have a concrete answer. A. I cannot give you a concrete answer, offhand. I would have to draft a summary.

Q. This is not offhand; you prepared it some weeks ago. A. Not the system of taxation of reciprocals; I have not prepared that.

Q. Is that the best you can do for me? A. Yes, it is the best I can do for you.

Q. Then, I shall have to be content. Another question: assuming that the \$4,000 I have mentioned hypothetically goes into the credit of a subscribers' account, and assuming that that were invested so that it bore income, what do you say about the liability of that income in the hands of the subscriber, or because it is in an account as credited to the subscriber, under the present Income Tax Act? A. I think that is earnings. It is his money, and he is liable to be taxed on the earnings on that money.

Q. And he is liable to be taxed, under present conditions, on it, is he not? A. Yes, that is quite correct.

Q. As an individual subscriber? A. Yes.

Q. Then, why do you tax anybody else other than the individual subscriber as to the earnings made on investment income? A. The only suggestion here is that the attorney-in-fact be assessed on income tax and excess profits tax.

Q. You are not answering my question, at all.

A. Well, I want to.

Q. I know you do, but probably we are both tired. I do not wish to be impatient; think about it a minute. You know that under this system of reciprocal insurance all the moneys that come to subscribers at an exchange are apportioned to the subscriber, and are credited to their individual accounts. A. Yes, that is the function of the exchange.

Q. And you know it is a probability that each subscriber has an individual account? A. Yes.

Q. If a proportion of that money, the \$4,000 I have mentioned in this case, is credited to the subscriber's account, and it earns income by being invested, then under present conditions that subscriber, although he has not got that money in his pocket -- it is income within the meaning of the Income Tax Act today, is it not?

A. I would like to be sure of that.

MR. PARKER: There is no evidence of it.

THE WITNESS: I do not know whether it is or not.

BY MR. MASON:

Q. All one has to do is to look at the Income War Tax Act. I do not like my learned friend's interruption, where he says there is no evidence of it, because one has only to look at the Income War Tax Act to see whether or not that is correct. And, while I am not arguing, I put it to you that it is futile to speak of investment

income of what you call an exchange, because that investment income is to the credit of individual subscribers, and the individual subscriber must have his own account with the taxing authorities of the government as to the amount for which he is responsible. Do you agree with that? A. Yes.

Q. Then, do you agree with me further that when you tax as you are suggesting in your brief, the effect would be to make the insurance much more expensive to the individual subscriber? A. I do not think there is any question about that.

Q. I did not think there could be. And just let me clarify one other point. You say -

"That the attorney-in-fact be assessed to income tax and excess profits tax in respect of the income and business profits of such organization remaining in his hands."

What do you mean by that? What are you going to tax? Are you going to tax the corpus or the income received from the corpus? Let us take the \$4,000 again; are you going to apply the income tax and the excess profits tax to \$4,000, or to the income from \$4,000? A. All we are talking about is income. It would be what portion of income would remain in his hands; either he pays it, or the subscriber pays it.

Q. In the instance we gave the \$4,000 is placed to his credit. You are not suggesting that income tax and excess profits tax be levied on the \$4,000? A. Yes.

Q. You are suggesting that this tax be attributed to the income from the \$4,000? A. Yes.

Q. My suggestion is that that \$4,000 -- at least that income goes to the credit of the individual subscriber

and is a matter for which he is already responsible.

A. I do not know whether he is responsible until he gets it, or when it is credited to him. I would have to look that up.

Q. I understand at least to some extent what you have in mind with respect to what is equitable, but I still do not understand it clearly. A. When that was written I did not know as much about reciprocals as I do now.

Q. Are you responsible for paragraph B yourself?
A. No, in consultation.

Q. Is there somebody else who can tell us more about paragraph B than you can? A. Not unless Mr. Mann can.

MR. MANN: And Mr. Mann will not be a witness, I do not think.

BY MR. MASON:

Q. Do you agree that the science or art, or whatever you call it, of insurance, has progressed greatly during the last twenty years? A. I do not know whether it is a science or an art; and what is progress?

Q. That is why I used both terms. A. What is the significance of the question?

Q. There has been a good deal of development in respect of the various types of coverage, and so on.

A. Yes, as to the scope of cover.

Q. Would you think the best thing to give the Commission, as evidence of what is now the proper thing to do in respect of insurance, is something which was done in Illinois in 1911 or in Toronto in 1916 or 1918?

A. Certainly not, if they were dealing with a form of cover. But that was not the purpose of the commission in Illinois.

Q. We will not worry about that. I think you have agreed in your brief with the suggestion that in a reciprocal exchange subscribers are both insurers and insured.

A. Where do I agree with that?

Q. You say that at page seven. A. Yes, I remember that.

Q. And do you agree with that? A. Yes, this is possibly the exception.

Q. Is it an exception, or is it not? A. That they are both insured and insurers?

Q. Yes, both insured and insurers. A. Yes, that is correct, I think.

Q. Then, you had some controversy with my learned friend Mr. Haydon about whether there was a fixed premium in the case of the Mutual Alliance? A. Yes.

Q. Do you say there is a fixed premium in the case of reciprocal exchanges? A. I would want to give consideration to that question.

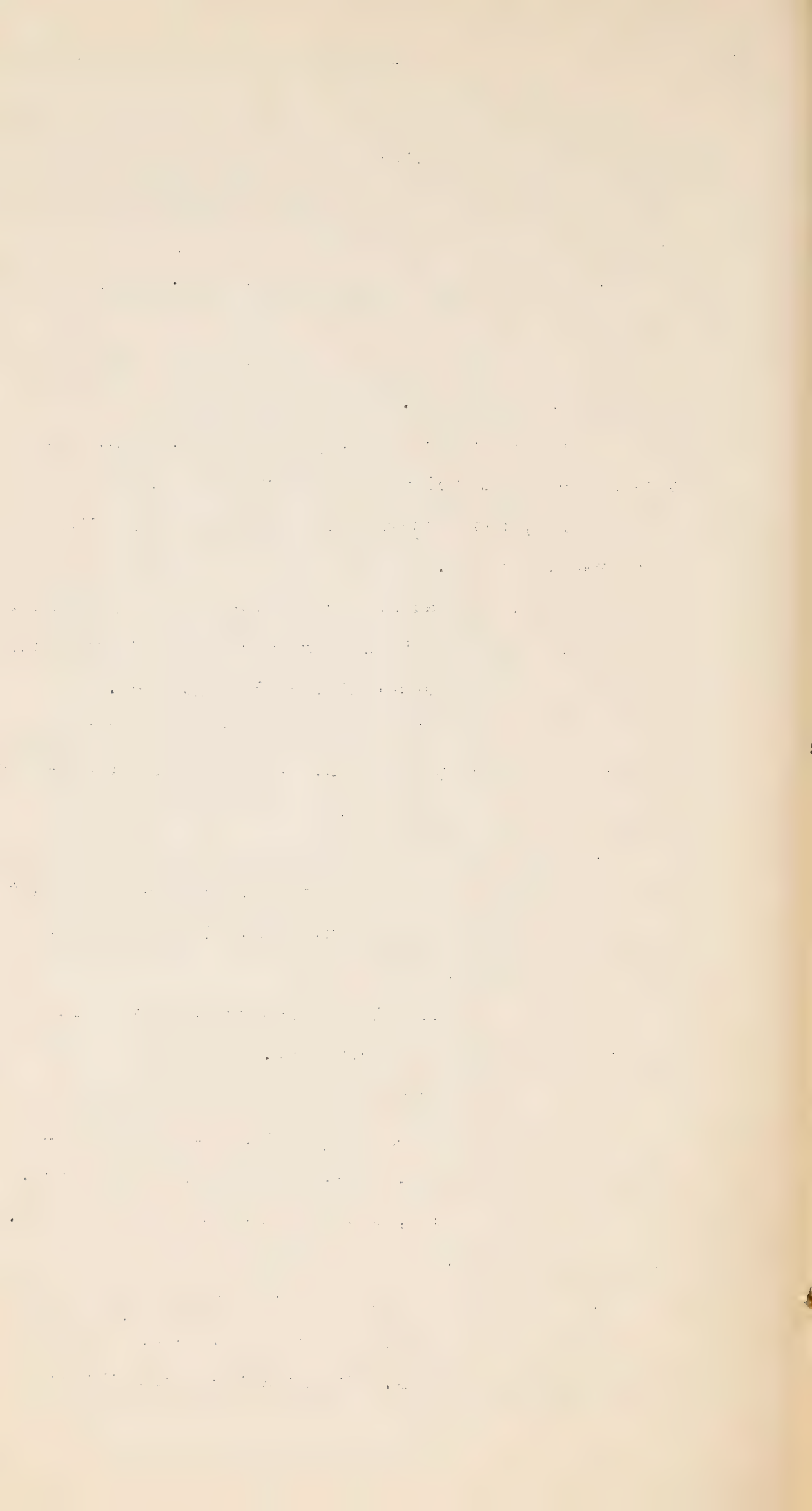
Q. Do you not know that the provisions of the contract do deal definitely with the allocation which must be made of the moneys paid in? A. I would have to study the contract.

Q. You would not like to answer it now? A. No, not without studying the contract.

Q. You do say somewhere in your brief that the destination of the money has not anything to do with the matter of taxation. A. Give me that reference.

Q. I think I can, but it would take me some time. A. I will find it.

Q. And you also said that you agreed with the principles as to insurance which are set out in the Thorvaldson brief. A. You mean the Income Tax Payers



Association?

Q. Yes. A. Yes, generally speaking.

Q. And this is really the point I should like to have discussed: you adopt this as your statement, as it appears at page six, paragraph ten, in that brief:

"In 1927 the House of Lords decided in the case of a company limited by guarantee and formed by employers to indemnify themselves against liability for fatal accident claims that the company's income was not assessable to tax on the principle of mutuality, although the company did not repay to its members the surplus receipts from premiums but carried them to reserve."

Do you agree with that? A. That is merely a statement of the court in the Southwestern Lancashire case, under the circumstances of that case. I believe there was such a case, and that such a decision was arrived at.

Q. Do you know of any decision which expresses any doubt as to that decision of the House of Lords -- well, perhaps I am dealing with a matter which should be discussed in argument. Then, one question further: have you, as a matter of fact, read the case to which reference is made in the brief, the case of Jones v. Southwest Lancashire Coal Owners Association? A. That is referred to there.

Q. And you have read the judgment in that case by Viscount Dunedin? A. Yes, but it was months ago.

Q. I shall not take the time to examine upon it, but I shall read a portion of it so that it may be drawn to the attention of the Commission. This is what we find at page 833, in 1927 Appeal Cases:

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Mr. Ham

"The whole case for the Crown rests on the idea that because in a single year the premiums received exceed the sums paid in respect of the losses in that year the balance represents a profit. It represents no such thing. It is simply a sum of money which is carried forward in order that it may be available to meet expensive losses in a future year, or if it is found in the end to be redundant, be returned to the shareholders either in the form of reduced premiums or of cash. The basis of the Crown's case seems to me to fail, apart from the fact that I agree that the present case is absolutely ruled by the case of New York Life Insurance Company v. Styles."

THE CHAIRMAN: Well, it is delightful to get back to the law reports.

MR. MANN: And it would be more delightful if the circumstances of the case were related to the Commission.

MR. MASON: I could do that, but I will say this for the benefit of my learned friends who are not here, that in the judgment of Viscount Cave, Lord Chancellor, at page 833, he says:

"The fact, therefore, that the insured, who are also the insurers, carry on their business through a medium of a company, was properly treated as immaterial."

MR. MANN: There is a little matter of identity there, is there not?

MR. MASON: I think the witness has already described my identity, and that is sufficient.

THE CHAIRMAN: I think we have had sufficient for today, and we will resume tomorrow morning. At what time

do you suggest?

MR. PARKER: At whatever time the Commission thinks desirable.

THE CHAIRMAN: It will be at 9.30 again.

MR. MASON: I hope I will not be considered discourteous to the Commission if I leave tonight, although I should like to have participated further in cross-examination tomorrow.

THE CHAIRMAN: I think it would be unwise to proceed further this evening, because we are all somewhat jaded.

MR. ROBERTSON: I, too, hope that I will not be considered as being discourteous if I do not appear tomorrow to cross-examine. I do not think it will be necessary.

The Commission thereupon adjourned to meet Saturday April 21, at 9.30 a.m.

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